NATIONAL
MULTIFAMILY
HOUSING
COUNCIL

Tool: Incentives to Develop

THE HOUSING AFFORDABILITY TOOLKIT

Developed in Partnership with
HR&A Advisors

Incentives to Develop

Housing development incentives can expand, diversify, and accelerate the production of affordably priced rental housing.

What Are Housing Development Incentives?

Local policies designed to stimulate the development of housing. A local government may employ a variety of mechanisms to incentivize the development of housing, whether by altering regulatory restrictions or by providing direct and indirect forms of support. Whatever the mechanism, these incentives ultimately increase revenue streams or decrease costs for a given development, thus increasing a project's likelihood of being developed.

REGULATORY INCENTIVES

Flexibility around project approvals, development rights, density, parking, and design.

FUNDING INCENTIVES

Direct or indirect funding or financing, to ease development costs or operating expenses.

How Housing Development Incentives Work

Housing development incentives can improve housing affordability in two ways – a direct approach that provides incentives in exchange for lower rents and a supply approach that increases the supply of rental housing to reduce the demand pressure on existing units.

DIRECT APPROACH

A well-run direct incentive program can increase affordability by requiring a reduction in rent in exchange for a commensurate set of incentives. These incentives can be achieved through negotiations between the developer and the municipality or through established government programs.

SUPPLY APPROACH

A supply approach focuses on increasing the overall supply of housing by reducing the costs of development and making more development feasible. An increased supply can stabilize or reduce rents and decrease the likelihood that existing residents are displaced.

Incentive Policies Can Be Designed to:

Expand Production
More housing is built than otherwise feasible

Diversify Production
Incentives strive for an optimal housing mix and depth of affordability

Accelerate Production
Housing is built more quickly than otherwise feasible

Incentives Categories

Housing development incentives vary widely in format and purpose and can be combined to achieve a suite of benefits.

Two Types of Incentives

Regulatory incentives can be relatively inexpensive and straightforward to implement but can be less effective than direct funding in increasing new housing by large amounts. Some incentives include:

- Density Bonuses
- Flexible Design Standards
- Reduced Parking Requirements
- Accelerated Approvals
- By-Right Development

Funding incentives provide money directly or indirectly from public reserves. They can be significant, and even necessary, for project feasibility. Some incentives include:

- Reduced Fees
- Public Land
- Tax Incentives
- Public Funding

All Incentives Should Strive to Be:

MEANINGFUL

To be meaningful to the developer, the incentive should pass the "but for" test: "but for" this incentive, the housing would not have been developed.

To be meaningful for the community, the incentive should be leveraged to **target a locality's specific needs.**

TRANSPARENT, CONSISTENT, AND ACCESSIBLE

Developers and other participants must be able to **understand, anticipate, and access** both the benefits and the associated restrictions and requirements.

MARKET-APPROPRIATE

The incentive must reflect local needs and constraints, such as market demand, political climate, affordability needs, and local cost levels.

Density Bonuses

In markets that can support more units, additional density will increase overall supply and help to bring rents in line with local needs.

Incentive Format

Density bonuses allow more units of housing to be built on a site than would be allowed for under existing zoning regulations in exchange for a developer's provision of affordably priced units or other public goals. The "bonus" can be achieved through an increase in floor area ratio (FAR), a greater building height, decreased minimum unit size, or loosened setback requirements. Density bonuses typically allow for an increase of between 10% and 20% over a zoning code's baseline permitted density. In effect, for every affordable unit in a development, the developer is able to add a determined number of market-rate units to the development.

Density bonuses work as an incentive by increasing a project's overall revenue and decreasing per-unit development costs. Developers are able to build, and eventually operate or sell, more units than otherwise possible. Often, these additional units are market-rate units that serve to offset the lower levels of rental revenue derived from affordably priced units.

Density bonuses are one of the most common incentives offered to developers. The incentive is relatively inexpensive, is straightforward to implement, and effectively advances public and private goals.

Market Impact & Considerations

IMPACT

In appropriate markets, density bonuses can effectively improve affordability through both direct and supply approaches.

Density bonuses can directly incentivize the building of more affordably priced units, if the rent generated by the additional units allowed is sufficient to offset the affordability requirements.

Moreover, by adding more units than otherwise would be the case, the project also contributes more to the overall supply of rental units, which can improve affordability.

CONSIDERATIONS

Is the market strong enough to support the additional units? A density bonus is not helpful if the additional units are left unabsorbed by the market.

Will the additional density alter the type of construction required for the building and, therefore, add exceptional costs? On a project-by-project basis, an increase in the number of units may trigger a need to use different construction materials. The potential increase in costs may nullify the increased revenue.

San Diego, CA's Affordable Homes Bonus Program (AHBP)

San Diego introduced a density bonus program that offers a maximum 50% density increase when at least 15% of units are rent-restricted. The AHBP also allowed developers to receive up to five density bonuses, rather than the three allowed by the state's analogous program. The AHBP received 18 applications within its first three months, marking a 900% increase in average monthly applications over submissions to the state density bonus program.

Flexible Design Standards

Flexible design allows for more housing to be built in places where it is most needed and reduces the cost of development.

Incentive Format

Design flexibility incentives reduce regulatory constraints, allowing for more flexible building designs. These incentives often entail reducing required setbacks, increasing buildable area, allowing for flexible lot consideration, or reducing minimum lot size requirements. Together, these design allowances increase the potential for development on infill sites, making use of a greater portion of urban land to provide housing.

By increasing the effective supply of developable land, flexible design standards work as an incentive by increasing project feasibility and unlocking potential revenues. Developers are able to build on land that would otherwise be unsuitable for housing if baseline design standards were maintained. Moreover, more challenging parcels of land that warrant design flexibility are often small infill sites in densely developed areas, where there is likely greater demand for housing. Flexibility incentives provide resident households the option to live in highly sought-after areas where there may be superior employment opportunity, public education, or transportation connectivity.

Market Impact & Considerations

IMPACT

Flexible design standards can contribute to affordability through both a direct and supply approach. Design flexibility incentives can be used to directly incentivize the addition of more affordably priced units. Moreover, by activating sites that would otherwise be unused, the incentive contributes to the overall supply of rental units, which can improve affordability.

CONSIDERATIONS

Is the market strong enough to support the additional units? In markets where units are not easily absorbed, the risks associated with the potential revenue may not justify the costs of undertaking an exceptional design.

Will the required changes in design lead to prohibitively high costs? On a project-by-project basis, the need for an unconventional design may cause a project to be costlier than is feasible.

A Suite of Design Incentives in Tallahassee, FL

In exchange for requiring 10% of new housing units to be affordable, the City of Tallahassee provides housing design flexibility, such as relief from setback requirements and minimum lot size requirements, as well as a 25% density bonus.

Reduced Parking

Relaxed parking requirements can decrease costs and allow more rental units to be developed.

Incentive Format

Reduced parking requirements relax zoning standards to allow for less required on-site parking, in return for the provision of more housing units.

Reduced parking requirements reduce costs and can potentially increase revenues. Structured parking is expensive to build, and surface lot parking is space-intensive. The flexibility to build only the parking space the market demands can amount to a significant reduction in construction costs and/or land costs. Moreover, it may be possible and market-supportable to use the saved space to build additional housing units, thus further increasing project revenues.

Market Impact & Considerations

IMPACT

Reduced parking requirements can contribute to affordability through both a direct and supply approach.

By requiring that projects provide a certain number or percentage of affordably priced units to qualify for the cost savings of reduced parking, the city may directly encourage an increase in affordably priced units. The lower costs of development can lower the necessary rent levels.

In addition, simply being able to build more housing units on space that would have otherwise been used for parking increases the overall supply of housing, thus easing rents through a supply approach.

CONSIDERATIONS

Are the levels of parking required reflective of market demand? A reduction in parking requirements should meet local demand for parking, amending what may be excessive requirements. As transportation options, such as ride-sharing, expand in some markets, local demand for parking spaces may meaningfully decrease.

How much costs do parking requirements add to development? The costs vary from market to market and by parking type but are significant in most areas.

Eased Downtown Parking Requirements for Seattle, WA

Seattle passed a bill in 2018 to reduce parking requirements for affordable housing projects, requiring one parking space per six units instead of three. In areas where “frequent transit” is available, no parking is required for any residential units. This measure will significantly ease rents in what is currently an expensive place to build – according to a 2015 report, one parking space per affordable housing unit increases rent by 12.5% in King County.

Accelerated Approvals

Saving time during pre-development and construction reduces both development costs and risks.

Incentive Format

Accelerated approvals move projects through key regulatory phases more quickly than usual. This may entail moving a project more quickly through initial land use approvals and post-entitlement planning or more expediently performing late-stage building code and construction inspections prior to delivery. Municipal staff may negotiate a timeline with the developer and may choose to prioritize projects and scale the approval timelines by each project's number of affordably priced units or depth of affordability.

Accelerated approvals work as an incentive by decreasing both the direct and opportunity costs associated with time and risk. By sticking to an expedited schedule, developers can avoid cost overruns and unnecessary delays, begin leasing units earlier, and obtain rental income sooner. Moreover, the resulting decrease in risk for a project may help developers access additional, or more favorable, sources of financing, decreasing necessary rents.

Market Impact & Considerations

IMPACT

Accelerated approvals contribute to affordability by directly reducing the cost of development, which allows for lower rents. Many cities promise to expedite reviews for projects that directly contribute to the city's stock of affordably priced units. The incentive is generally most effective in securing affordably priced units if provided alongside additional incentives.

CONSIDERATIONS

Is the incentive adequate on its own? Accelerated approvals alone are unlikely to "move the needle" on housing development. However, the incentive is relatively inexpensive and straightforward to provide, and when effectively delivered it models a general good practice for efficient government. The incentive can be especially effective in certain markets where risks are high or for certain projects or developers particularly sensitive to delays.

Accelerated Permitting in Santa Fe, NM

The City of Santa Fe, New Mexico accelerates the permitting process for projects that include at least 25 percent affordable housing. This policy is coupled with a number of other ordinances, including permit fee waivers, impact fee waivers, and a reduced utility expansion charge for affordably priced housing properties.

By-Right Development

Housing supply can grow in response to demand, helping to bring rents and housing options more in line with community needs.

Incentive Format

A by-right development approval process uses uniform, codified, and consistent zoning and development regulation to streamline and enable new housing developments. In contrast, "discretionary" zoning allows disparate groups to prioritize individual interests in ways that can be severely disruptive to the addition of housing supply and affordability.

By-right development works as an incentive by reducing softs costs and land costs and by mitigating project risk. An efficient and predictable entitlement process reduces carrying costs, consulting fees, and other costs associated with approval processes when compared to a lengthy discretionary review process. Land costs are reduced when the zoning premium on multifamily land is rendered obsolete, as by-right policies increase the number of parcels with few zoning restrictions, reducing competition and associated land costs.

Market Impact & Considerations

IMPACT

By-right development lowers the cost and increases the supply of rental housing in areas where there is the greatest demand, thereby reducing the competitive pressures that drive up rents. By decreasing the costs associated with permitting and entitlement, developments require less financing and lower rents to achieve viability. By-right development protocols also encourage a greater volume of new development, as developers can anticipate a transparent and efficient process.

CONSIDERATIONS

Does the market need more units? By-right development allows supply to be more responsive to demand or actual need.

Is there political will to adopt by-right development? By-right development requires political consensus, which can be difficult to achieve in many jurisdictions.

How does the building review process differ geographically? Areas where discretionary review is more stringent, and where communities are more well-organized, tend to be wealthier and more well-established communities where affordably priced housing is most needed.

"The Anti-Snob Law" – Massachusetts Chapter 40B

Once achieved, a statewide approach to by-right development both reflects and can act upon broad coalitions of support for more housing. The state of Massachusetts passed Chapter 40B in 1969, which allows affordable housing to be developed in towns where less than 10% of housing is affordable, regardless of local zoning ordinances. The policy has reduced local zoning and permitting barriers. 90% of qualifying projects submitted to local Zoning Boards of Appeals have been approved.

Reduced Fees

Waivers or reimbursements decrease costs dollar-for-dollar, while deferrals reduce risk.

Incentive Format

Fee reductions waive, reimburse, or defer a variety of fees typically incurred throughout a project's lifespan. These fees include those associated with building permitting, planning, and development, such as zoning fees, subdivision fees, site plan fees, building plan review-permit-inspection fees, and impact fees.

The extent of the fee reduction can be scaled depending on the type of housing units in question. For example, fees may be reimbursed to different percentages depending on the depth of affordability. Another policy option is to defer fees for market-rate units, such that the fee is to be paid when those units reach a certain level of occupancy.

Fee reductions work as an incentive by directly decreasing project costs (or project risk, in the case of fee deferrals). Fixed cost savings are especially valuable for smaller developments, and per-unit cost savings can be significant for larger developments with many housing units.

Market Impact & Considerations

IMPACT

Reduced fees contribute to affordability primarily through direct cost reduction.

Fee reductions cover development soft costs and, therefore, help to lower the rents that a project requires to be feasible and profitable.

In some markets, a large fee reduction may be adequate to instigate a greater volume of housing development, but the incentive does not often contribute to a significant growth in supply.

CONSIDERATIONS

How meaningful are fee reductions in a market? Fee reductions would be most impactful in markets where developers are already eager to build but where development costs are high enough for a waived fee to be significant.

How important are these fees to the property and community? Some fees, such as impact fees, would contribute to surrounding infrastructure and improvements. Foregoing this capital to incentivize affordability forces a tradeoff between important public goods.

Impact Fee Waivers in Polk County, FL

Polk County waives and reduces impact fees for newly developed for-sale and rental units provided to low-income households. Developers pay full impact fees up front when applying for a permit, but fees are reimbursed as housing units are occupied by low-income households. The county sets a maximum waiver cap of $250,000 per year across the city, to limit the program's impact on the city budget.

Public Land

Public land sold at a below-market price in exchange for affordability lowers the cost of development and allows for lower rents.

Incentive Format

A public land policy establishes criteria by which local governments select and sell parcels of publicly controlled land at below-market prices (often free) to improve affordability. Effective policies draw from a broad portfolio of land parcels and work to maximize the value of that land – such as by allowing for dense and mixed-income developments. The policy should employ a well-defined selection process and expedient regulatory approvals.

Public land acts as an incentive by decreasing development costs. The reduction in land price mitigates a very significant development cost, allowing for lower rents and greater affordability.

Public land disposition can operate effectively and create community benefits in strong and weak markets alike. Disposition creates opportunities in strong markets and catalyzes reinvestment in weaker ones.

Market Impact & Considerations

IMPACT

Public land incentives can contribute to affordability through both direct and supply approaches. By minimizing a significant cost to development, public land incentives directly allow for the creation of more affordably priced units. And depending on the market need, public land can be provided as an incentive for a spectrum of housing types, to contribute to the overall supply of rental units, which can improve affordability.

CONSIDERATIONS

What is the size and strength of a municipality's public land portfolio? The impact of this incentive is directly tied to quantity and quality of land made available. More and better-quality parcels have a greater impact on affordability.

Is the incentive complemented by other policies? Public land incentives typically are not effective on their own. Even with a significant portfolio, a standalone land policy will produce fewer than 100 units annually.

High Density Transit-Oriented Workforce Housing in Atlanta, GA

Atlanta's public land disposition guidelines are complemented by zoning relief for project modifications, as well as higher density uses and reduced parking requirements. These offerings helped the Metropolitan Atlanta Rapid Transit Authority (MARTA) recruit developers for station-area transit-oriented development (TOD) contracts that include workforce units. The program, introduced in Q3 2018, is coupled with a $15 million fund that will provide below-market, low-rate financing to support development of workforce housing.

Tax Incentives

Property tax incentives improve affordability by lowering the cost to operate rental housing.

Incentive Format

Property tax incentives are state or local policies that reduce the tax burden on properties that support a public policy goal. The specific mechanisms vary but fall under three broad categories: tax abatements, tax rebates, or tax exemptions. These incentives can be strategically enacted in different geographies and for different project types, to encourage development for which the city has the greatest need. For example, tax incentives can be provided for both new development and for capital improvements on existing buildings.

These tax incentives work by reducing property taxes, lowering operating costs. For a designated period of time, tax reductions amount to a direct discount on a property's operating costs. As operating costs rise in many areas, this cost savings can be very meaningful for project budgets.

Market Impact & Considerations

IMPACT

Tax incentives can effectively contribute to affordability through both a direct and supply approach. By lowering operating expenses, tax incentives directly allow for projects to incur lower rents, as is often required. And in markets where the promise of tax incentives is enough to encourage more development overall, the incentive contributes to affordability by increasing housing supply.

CONSIDERATIONS

Can a municipality afford the cost of foregone revenue? A direct approach to improving affordability can work in any market, as long as the city is able to bear the opportunity cost of lower tax revenues.

Would other market conditions prevent the efficacy of tax incentives? Tax incentives would be most effective in markets where rents do not support construction costs, but where land is largely available and developable. If a city's land use and regulatory environment is the primary barrier, tax incentives will not be able to induce new development.

Inducing Development in Philadelphia, PA

Philadelphia's tax incentive policy is designed to induce development of for-sale and rental housing by applying a significant 10-year tax incentive to a market with relatively weak conditions and the fourth-highest construction costs in the country. As a result, development has increased by 367% since the incentive took effect in 2000, while suburban areas without the incentive saw only an 11% increase in building activity. A report by JLL found that every $1 in tax revenue foregone results in $2 of net revenue through the resulting effects of the policy.

Public Funding

Public money can catalyze development that would otherwise be financially infeasible.

Incentive Format

Public funding "closes the gap" for desirable but otherwise infeasible projects. This money can come from federal, state, and local levels, with a multitude of formats and restrictions. Meaningful funding levels typically range from hundreds of thousands to millions of dollars.

Funding can be invested *directly* into project costs (capital or operating). In this case, the incentive works by directly decreasing costs and expenses. Public money often constitutes a critical piece of the capital stack for developers of affordably priced housing.

Funding can also *indirectly* benefit a housing project by covering the costs of surrounding improvements. These amenities include transportation and utilities infrastructure, parks and open space, and investments in economic revitalization. These projects bolster the success and cash flow of not only the project, but also the community and future projects.

The promise of public money serves as an early-stage instigator for new housing projects. Funding can be competitive to secure and tightly budgeted, but – when properly allotted – can be transformational for funding recipients.

Market Impact & Considerations

IMPACT

Public funding contributes to affordability through both a direct and supply approach. Depending on the source, public funding is often competitively awarded to projects that promise to deliver affordably priced units. This is possible because the funding directly reduces development costs and, therefore, the rents necessary for a viable project. Public money and improvements also play an important role in galvanizing new development of all kinds, thus improving affordability by increasing supply overall.

CONSIDERATIONS

What restrictions does the public funding take? Depending on their design, public funds can come with many strings attached, which can affect the project's calculus in direct and indirect ways.

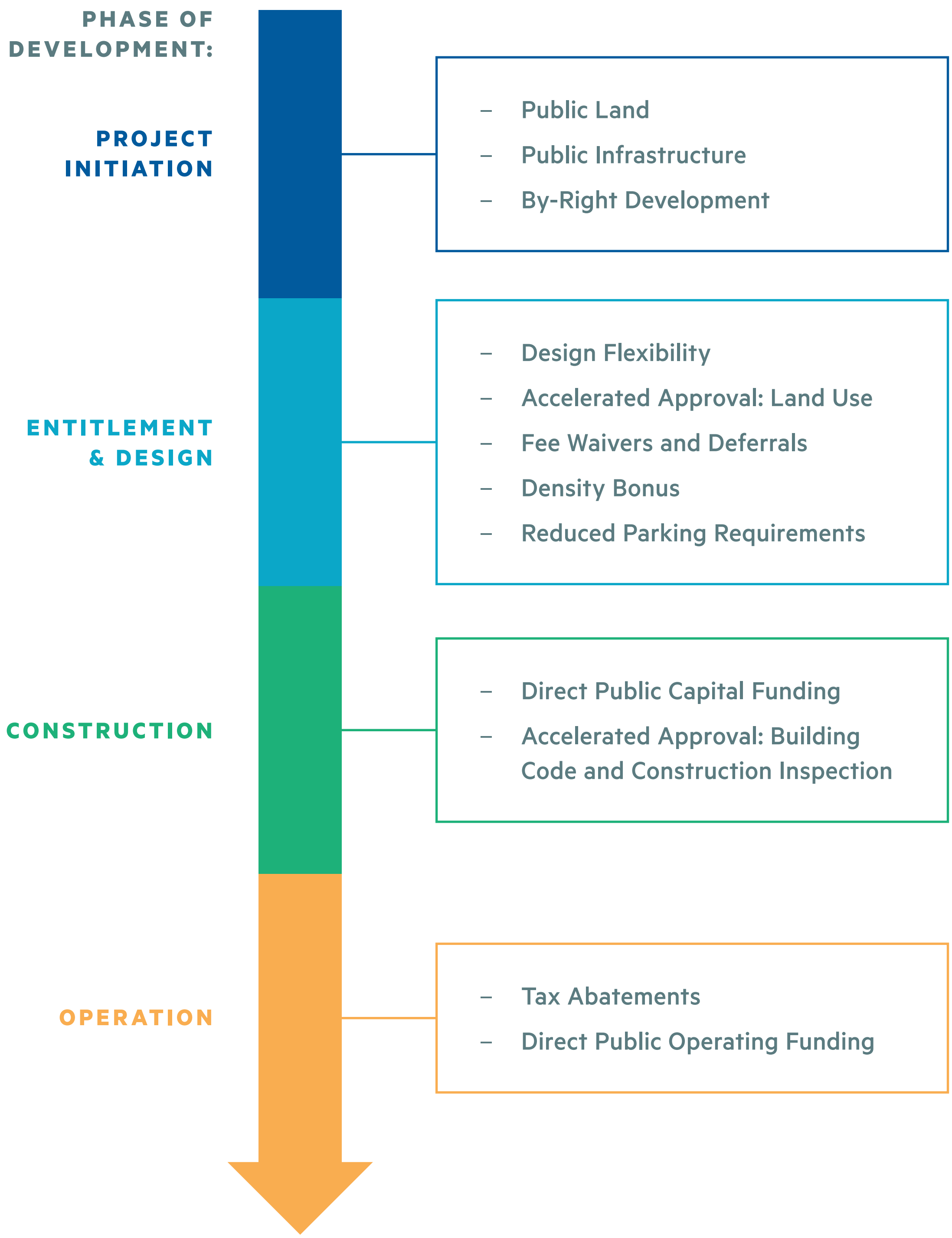
How significant is the financing gap, and will public money be adequate to fill it? In markets where building is expensive and/or rents are weak, a significant level of funding may be necessary – and public reserves may be inadequate.

Housing Production Trust Fund in Washington, D.C.

The HPTF is a special revenue fund in the District of Columbia that produces and preserves affordable housing. Drawing from a 15 percent tax on deed recordation and transfer taxes, the fund currently aims to commit $100 million per year (the second highest in the nation). Every dollar of HPTF funding is matched with $2.50 of private and federal financing, to be used toward qualifying and winning projects that serve a stipulated range of AMIs and housing needs. Between 2001 and 2016, the HPTF produced or preserved nearly 10,000 units of affordable housing.

Phases of Incentives

Housing incentive policies influence project financials and outcomes throughout the development process.

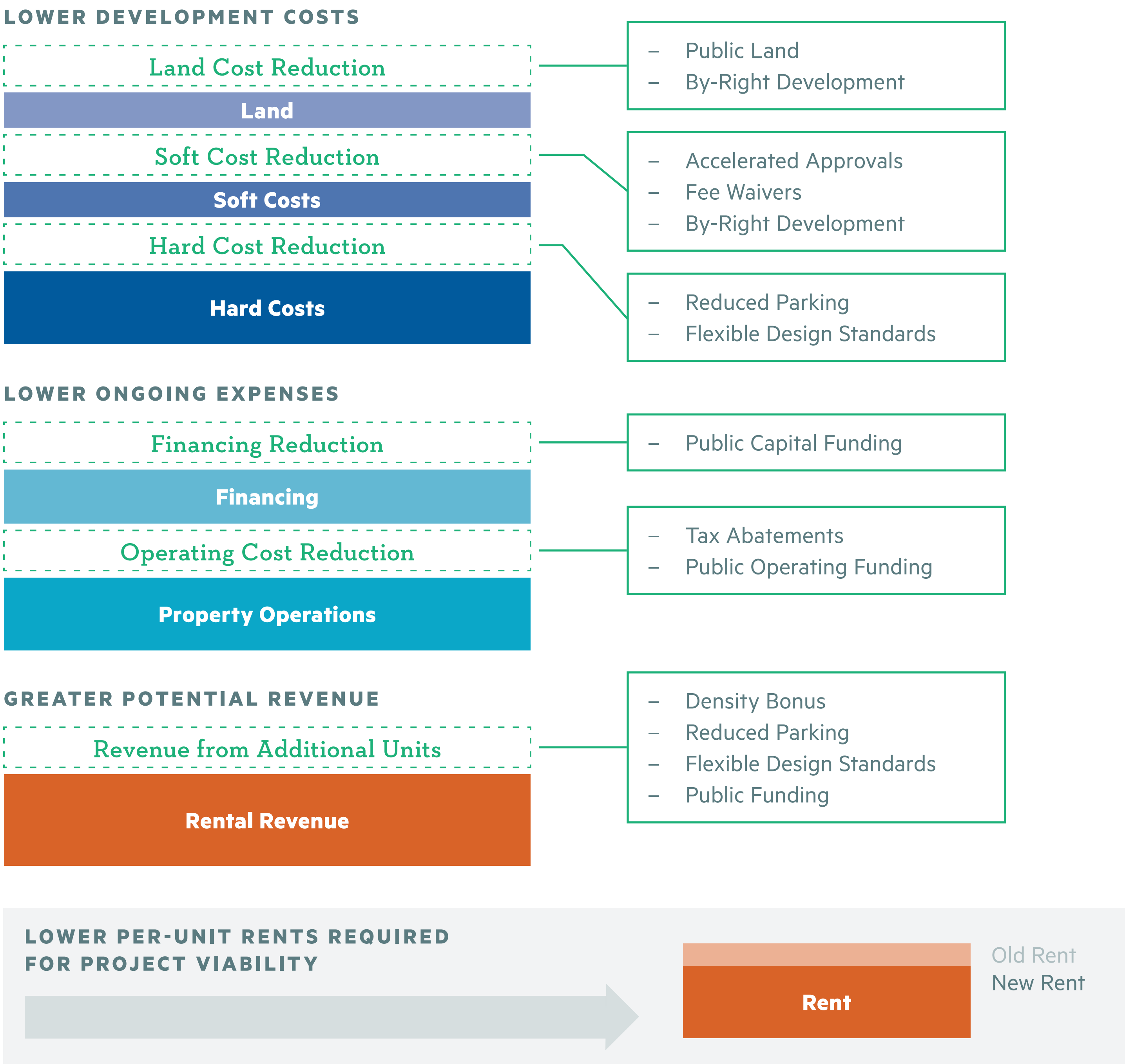


Economics of the Tool

Housing incentive policies can obligate and/or allow for a direct reduction in rents.

Direct Approach: Reduced Costs and Expenses; Increased Revenue

Housing development incentives reduce costs or increase revenue, thus allowing for a direct decrease in rent for at least a portion of units, while still maintaining project viability.



Economics of the Tool

Housing development incentives can be designed to increase the production of all forms of housing.

Supply Approach: Increasing Overall Production

Housing development incentives can increase the supply of housing and, consequently, improve housing affordability. In particular, **incentives such as by-right development, flexible design standards, public land, public funding, and tax incentives can significantly increase the likelihood of development.**

Currently, the increase in rents of existing affordably priced market-rate housing is one of the largest factors driving the affordability crisis nationwide. The loss of this housing is a direct result of insufficient supply for new renter households. Increasing the supply expands affordability for all households.

The indirect impact of increased supply on lowering rents can be significant. Below is the estimated[1] impact of a 1% increase in housing supply on rents and the number of households who would be able to afford rental housing as a result.

	DECREASE IN SHARE OF UNITS <$800 SINCE 2000 (PERCENTAGE POINTS)	EFFECT OF 1% INCREASE IN SUPPLY: REDUCTION IN RENT	EFFECT OF 1% INCREASE IN SUPPLY: INCREASE IN AFFORDABILITY (BY HOUSEHOLDS)
Atlanta	15.7	0.63%	690
Sacramento	19.5	0.98%	720
Minneapolis	15.1	0.95%	780
Denver	20.9	0.98%	1,300
Pittsburgh	21.1	1.19%	730
San Antonio	19.3	0.82%	720
Seattle	14.5	1.02%	1,500
Tampa	26.8	1.00%	580

A **1% increase** in overall supply in Pittsburgh would add **1,200 units** to the market and reduce overall prices by **1.19%**. This would make Pittsburgh affordable to **730** additional households.[2]

1 A 2018 study by the Bay Area Council Economic Institute ("Solving the Housing Affordability Crisis") evaluated the effect of various housing policies based on the number of households for which housing would become affordable as a result of the policy, using a 30% housing-cost-burden assumption. The report evaluated the responsiveness of price to changing the supply through policy. Using a similar method, HR&A evaluated the number of households for which housing would become affordable, given a 1% increase in the overall supply of the eight case-study cities.

2 730 additional households would pass the threshold below 30% for affordability.

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Tool: By-Right Development

THE HOUSING AFFORDABILITY TOOLKIT

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By-Right Development

Establishing by-right development allows the supply of housing to grow with demand and helps to stabilize and lower rents.

What Is By-Right Development?

A housing development policy that prioritizes the development of higher density multifamily housing through uniform, codified, and consistent zoning and development regulation.

HOW BY-RIGHT DEVELOPMENT WORKS

A by-right development approval process establishes a rule-based development approval process that improves the ability of the housing market to create new housing in response to increased demand.

BY-RIGHT DEVELOPMENT IMPROVES AFFORDABILITY IN TWO WAYS:

1. Lowers the cost of development through a faster, more predictable approval process.
2. Increases the supply of housing.

Faster, more predictable approval processes lower the cost to obtain development approval, reducing overall development costs. Creating new housing increases the supply of housing and reduces competition between new and long-time residents for existing housing.

> **“All neighborhoods benefit in the long run if they allow for the production of new housing units.”**
>
> – Mark Willis, Senior Policy Fellow, NYU Furman Center

RULE-BASED VS. DISCRETIONARY

A rule-based approach clearly outlines the permitted use, shape, and density at a parcel level. When development projects are submitted, review is administrative and does not exercise discretionary judgement on the project.

Conversely, a discretionary approval process gives increased power to legislative bodies and city staff to create conditions and requirements that are unique to specific projects.

NOT IN MY BACKYARD (NIMBY)

NIMBYs are individuals or organizations that oppose the development of new housing in their neighborhood. NIMBYs routinely use discretionary, non-rule-based development approval processes to block the development of new housing.

Effective Policies

1. Rely on rule-based approval process
2. Encompass a significant portion of the market
3. Apply to more desirable neighborhoods
4. Require strong political support

Recommendations

1. Effective by-right development relies on a rule-based approval process.

The development approval process should be predictable. Developers should be able to evaluate with confidence what types of developments will be approved, what types of requirements the community will impose, and how long approval processes will take. Predictability reduces the cost of development by reducing the cost of obtaining development approvals and allows developers to focus on projects that will be approved, increasing overall supply.

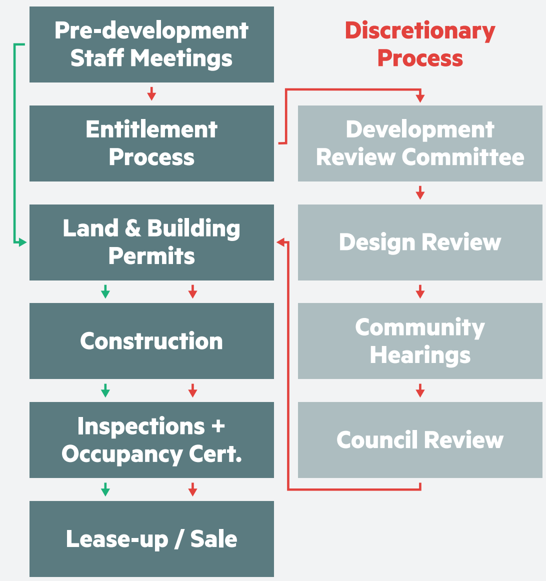
By-Right vs. Discretionary

Most cities exist on a spectrum between rule-based zoning and discretionary zoning. A rule-based approach clearly outlines the permitted use, shape, and density at a parcel level. When development projects are submitted, reviews are administrative and do not exercise discretionary judgement on the project. If all the zoning and code requirements are met, approval must be given for the project.

Conversely, a discretionary approval process gives increased power to review boards, elected officials, and city staff to create conditions and requirements that are unique to specific projects.

Most discretionary approval processes create a series of discretionary reviews, each of which can block development or increase costs. The development map to the right represents a typical development process distilled from a literature review of multifamily development processes across the country. Any one of the reviews can be used by NIMBYs to prevent the development of additional housing.

Typical Development Process Map



An effective by-right development process limits discretionary reviews. Every discretionary review can decrease the potential housing supply, either by blocking projects or reducing their size. A restricted housing supply contributes to affordability challenges. Communities may choose to include some additional discretionary reviews related to key public policy goals. But to keep the affordability benefits of a by-right approach, the number of reviews must be limited.

> “Design guidelines should control only those elements of design that don’t affect the basic entitlement."
>
> – Los Angeles ReCode, 2014

Recommendations

1. Effective by-right development relies on a rule-based approval process.

Discretionary reviews in the development approval process should have well-defined criteria that set high thresholds for intervening in a proposed housing development. Discretionary reviews often use broad jurisdiction to interpret development standards. This flexibility allows NIMBYs to stretch the purpose of discretionary reviews and block new housing, often based on issues beyond the intended purpose of the review.

Design Review Roadblocks

A review of Los Angeles's zoning code[1] showed that the city often requires a lengthy urban design review process for multifamily buildings. This design review was often used as a tool by those that opposed new housing to limit zoning approvals and directly undermine the city's housing affordability goals.

An effective by-right process can still include minor additional discretionary reviews for extremely large projects. A catalytic redevelopment of a city block or a development proposing 1,000 or more units may meet this threshold. **However, only a very small portion of multifamily developments would meet the threshold; most should be approved through a rule-based process.** Local governments tend to set low thresholds, resulting in required discretionary reviews for a significant portion of large projects.

Although the implementation of a rule-based system is an important step in expanding by-right development, it can still be misused to restrict the supply of housing. The wealthy Silicon Valley suburb of Los Altos Hills has by-right zoning that only allows low-density, single-family housing and does not allow for any multifamily housing within city limits. The city does not contribute to the region's supply of housing, despite being adjacent to large and growing job centers.

"Large Project" Zoning Approval in Boston, MA

In Boston[2], any project larger than 50,000 square feet (40-45 units) requires a "large project review," which triggers a public comment period, reviews with interested City and State agencies, design review, and a negotiation process with the planning board. This has resulted in projects being "engineered" to fit the allocated 50,000 SF by reducing units, which artificially reduces Boston's housing supply. This process can take dozens of months and has created a cottage industry of consultants that manage multiple layers of review.

The process has three public review steps:

1. A Project Notification Form;
2. A Draft Project Impact Review analyzing the environmental, traffic, neighborhood, and other impacts of the project; and
3. A Final Project Impact Report in response to concerns raised during the public hearing.

At each point in this process, pressure from neighborhood groups can mount and halt or shrink the project, despite Mayor Walsh's housing goals in the Boston 2030 comprehensive plan.

A city's rule-based zoning policy must facilitate sufficient multifamily housing development to be an effective housing affordability tool.

1 Los Angeles ReCode, 2014
2 "What is Article 80?", Boston Planning and Development Authority

Recommendations

2. Effective by-right development encompasses a significant portion of the market.

The larger the scale of a by-right policy, the greater the potential impact on affordability. By-right development primarily impacts affordability by allowing the supply of housing to meet demand. Cities often restrict by-right multifamily development to a small area, substantially restricting the policy's ability to address affordability challenges. For a by-right policy to be effective, it must apply to a significant portion of the market.

Local governments need to understand the magnitude of projected growth and scale their by-right policies accordingly. Local governments should execute thoughtful planning exercises to predict the volume of growth and the location of high-growth areas prior to establishing the scope of by-right policies. When by-right development policies are not aligned with market conditions, they are far less effective at impacting affordability.

A regional approach to by-right development is often the most effective. Housing markets operate at a regional scale, so sole local governments may struggle to accommodate regional growth, even with a by-right policy in place.

> **"[SB 827]...could be "the biggest environmental boon, the best job creator, and the greatest strike against inequality anyone's proposed in the United States in decades."**
>
> – Boston Globe, June 2018[1]

"A Statewide Upzone" – SB 827

In 2016, the McKinsey Global Institute found that California needed to build 3.5 million homes by 2025[2] to address pent-up demand and stabilize rents across income groups.

A 2017 senate bill proposed by California State Senator Scott Wiener would have taken advantage of recently built transit infrastructure by enacting a statewide up-zoning to remove density limits and parking requirements on parcels within a ½ mile of high-speed transit. It was designed to override local zoning and set neighborhood maximum heights between 45 and 85 feet, depending on context.

An independent evaluation of the bill's impacts found that this would "significantly upzone nearly all of San Francisco to 45- and 85-foot heights (depending on distance to transit stops), as well as significant portions of Los Angeles, Long Beach, San Diego, Oakland and Berkeley." Another localized study found that metro stops in Oakland would be upzoned up to five times their current capacity.[3]

Although the bill did not pass, it struck a national chord by illustrating how by-right development is essential to addressing housing affordability.

1 Ramos, Dante, "Go on, California – blow your lousy zoning laws," 2018
2 Woetzel et al. "Closing California's Housing Gap" McKinsey Global Institute, 2016
3 DiStefano, "How Might SB827 Impact California?," 2018

Recommendations

3. Effective by-right policies apply to more neighborhoods with increased opportunities.

While development in all markets is helpful, developing new housing in strong areas has a larger stabilizing effect on a locality's rents than developing in weaker areas. **Neighborhoods with increased opportunities like good schools and amenities have the greatest demand.** They also tend to have more political and financial resources to use discretionary approval processes to block new housing. Moving to a by-right approach stops the misuse of discretionary reviews and leads to more housing development and more affordability.

> "Living somewhere that feels like the suburbs but is next to an express train."

DITMAS PARK, BROOKLYN

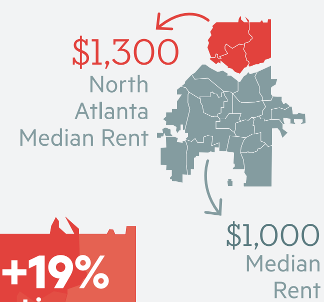
In order to reach the New York City's ambitious housing and equity targets, the Regional Planning Association (RPA) has recommended that the city up-zone and expand by-right development to all neighborhoods – including traditionally residential neighborhoods.[1]

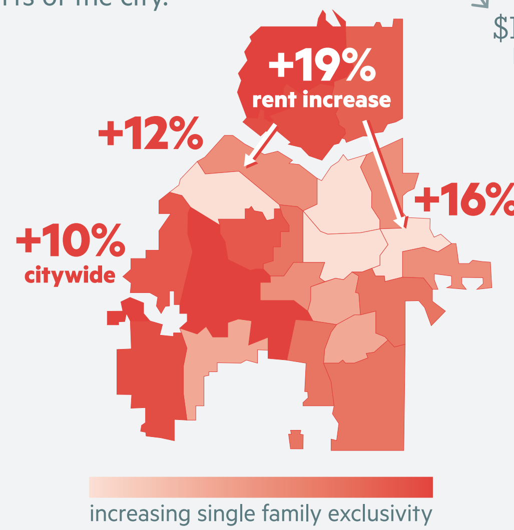
The RPA found that none of these "desirable" neighborhoods, defined by RPA as tracts with median incomes greater than $50,000, top performing elementary schools, and within 0.6 miles of subway access, were up-zoned since 2000, unlike other middle-income neighborhoods in Brooklyn and Queens. These neighborhoods effectively blocked all up-zoning attempts and maintain low-density communities, while the city lacks sufficient housing.

If development is blocked in desirable neighborhoods, it moves to lower-income, largely minority communities. The discretionary approval process and the lack of by-right development in high opportunity neighborhoods are rarely identified as culprits, but they play a key role in the process of displacement.

Demand for Housing in Desirable North Atlanta has Spilled Over to West and East Atlanta.[2]

95% of north Atlanta is zoned for single-family housing and is one of the most desirable parts of the city.





Development in north Atlanta has been constricted by zoning, shifting demand to adjacent parts of the city. This has resulted in greater displacement and decreased affordability in parts of west and east Atlanta.

1 "Is NYC as Transit-Oriented as We Think?" – RPA Lab, 2018
2 HR&A analysis, Atlanta Equitable Housing Study, ACS 2016 5-year survey

Recommendations

4. Effective by-right policies require strong political support.

Strong political will and leadership is required to establish and sustain an effective by-right development policy. NIMBYs will put pressure on elected and appointed officials to block by-right development that they believe will impact their quality of life.

There are a number of ways to create political support for by-right development and improve affordability. Local governments and concerned community members should pursue multiple approaches:

Encourage community support and Yes In My BackYard (YIMBY) groups that advocate for increased development and multifamily housing to stabilize rents and improve affordability. These groups can be valuable partners of local governments and help spread awareness about the link between by-right development, increased supply, and greater affordability. Several of these groups have formed across the country, with active members in many cities facing high levels of discretionary zoning like Los Angeles, San Francisco, and Cambridge.

Review existing efforts to promote statewide by-right development. This is a drastic measure but may be necessary to overcome local opposition to new housing. A statewide approach takes the issue out of the hands of local elected officials and allows for the formation of broader coalitions of support.

"The Anti-Snob Law"

– MASSACHUSETTS CHAPTER 40B[1,2]

The best example of this is the Chapter 40B "anti-snob law" in Massachusetts, which allows development of affordable housing to be built in towns where less than 10% of housing is affordable despite local town zoning ordinances. It was created in 1969 to reduce local zoning and permitting barriers to housing production and to encourage the production of housing in all communities throughout the state.

If certain conditions are met, developers are eligible to submit a comprehensive permit to the local Zoning Board of Appeals (ZBA). Projects are approved 90% of the time. If they are not approved, the developer can appeal to the state Housing Appeal Committee. In these cases, the burden of proof falls on the local ZBA to prove that the project "demonstrates a valid local concern that outweighs the regional housing need."

1 Interviews with Chapter 40B administrators

2 Reid et al. "Borrowing Innovation, Achieving Affordability: What we can learn from Mass. Chapter 40B," 2016

Considerations & Limitations

Efforts to improve affordability in a community must include some form of by-right development to be effective.

Impact

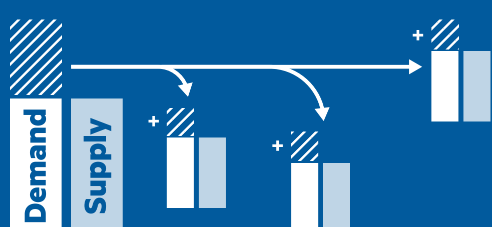
The reliance on discretionary zoning in place of by-right development restricts the supply of housing and decreases affordability for all income levels. Studies of the Bay Area, New York City, Boston, and Los Angeles have all found that sharp increases in zoning restrictions contribute to the current housing affordability crisis, exacerbate wealth disparities, and result in economic and racial segregation. The discretionary approval process allows NIMBYs to use traffic, school crowding, and environmental impacts of new housing to prioritize their quality of life over housing affordability for the broader community. Finally, by-right development reduces the potential impact of NIMBY groups on projects and communities.

> **“In 1960, Los Angeles was zoned to accommodate 10M residents and had a population of 2.5M. In 2016, the city was zoned for only 4.3M with a population of 4M.[1]”**

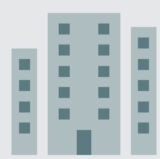
Market

Expanding by-right development is an effective strategy to increase supply and affordability in strong and weak markets alike. In both strong and weak markets, there are neighborhoods where there is demand for more housing. **It is most effective to expand by-right development in neighborhoods where demand pressure is the highest – this is where there is the greatest need for additional supply.**

When desirable neighborhoods restrict zoning and create excess demand, it causes demand pressure on adjacent communities, resulting in widespread rent increases and displacement.



Housing Goals



INCREASED HOUSING SUPPLY

INCLUSIVE, MIXED-INCOME NEIGHBORHOODS

When implementing housing policies, local governments may pursue a range of housing goals. Expanding by-right development is an effective strategy to **increase the overall supply of housing** by responding to demand increases. It can also create mixed-income neighborhoods, as cities undo the deleterious effects of exclusionary zoning and build in more desirable neighborhoods.

1 The White House (Obama Administration) Housing Affordability Toolkit, September 2016

Recommendations Summary

To design an effective by-right policy, a city should take a four-tiered approach.

1. EFFECTIVE BY-RIGHT POLICIES RELY ON RULE-BASED APPROVAL PROCESSES

- The development approval process should be predictable.
- Discretionary approval processes used by most cities create a series of obstacles – often in the form of multiple layers of discretionary reviews – to develop new multifamily housing.
- An effective by-right development process should include only a limited number of discretionary reviews.
- Although a rule-based system is an important step in expanding by-right development, it can still be misused to restrict the supply of housing. A city's rule-based zoning policy must facilitate multifamily housing development to be an effective tool in stabilizing and reducing rents.

2. EFFECTIVE BY-RIGHT POLICIES ENCOMPASS A SIGNIFICANT PORTION OF THE MARKET

- The larger the scale of a by-right policy in terms of where it applies within a jurisdiction, the greater the potential impact on affordability.
- Local governments need to understand the magnitude of projected population growth and scale their by-right policies accordingly.

3. EFFECTIVE BY-RIGHT POLICIES APPLY TO MORE DESIRABLE NEIGHBORHOODS

- By-right development policies have the greatest impact on housing affordability in high-demand neighborhoods by reducing the competition between existing residents and new residents for a limited supply of housing.
- Moving to a by-right approach stops abuse of discretionary processes and leads to increasing housing development in desirable areas.
- When desirable neighborhoods reject by-right policies, new housing development concentrates in lower-income and minority communities, driving displacement.

4. EFFECTIVE BY-RIGHT POLICIES REQUIRE STRONG POLITICAL SUPPORT

- Strong political will and leadership is required to establish and sustain an effective by-right development policy.
- Encourage Yes In My BackYard (YIMBY) groups that advocate for increased development and multifamily housing.
- In strong markets, tie by-right policies directly to the production of units with below-market-rate rents.
- Consider regional or statewide policies mandating by-right development when necessary to overcome local opposition to new housing.

By-Right Development Economics

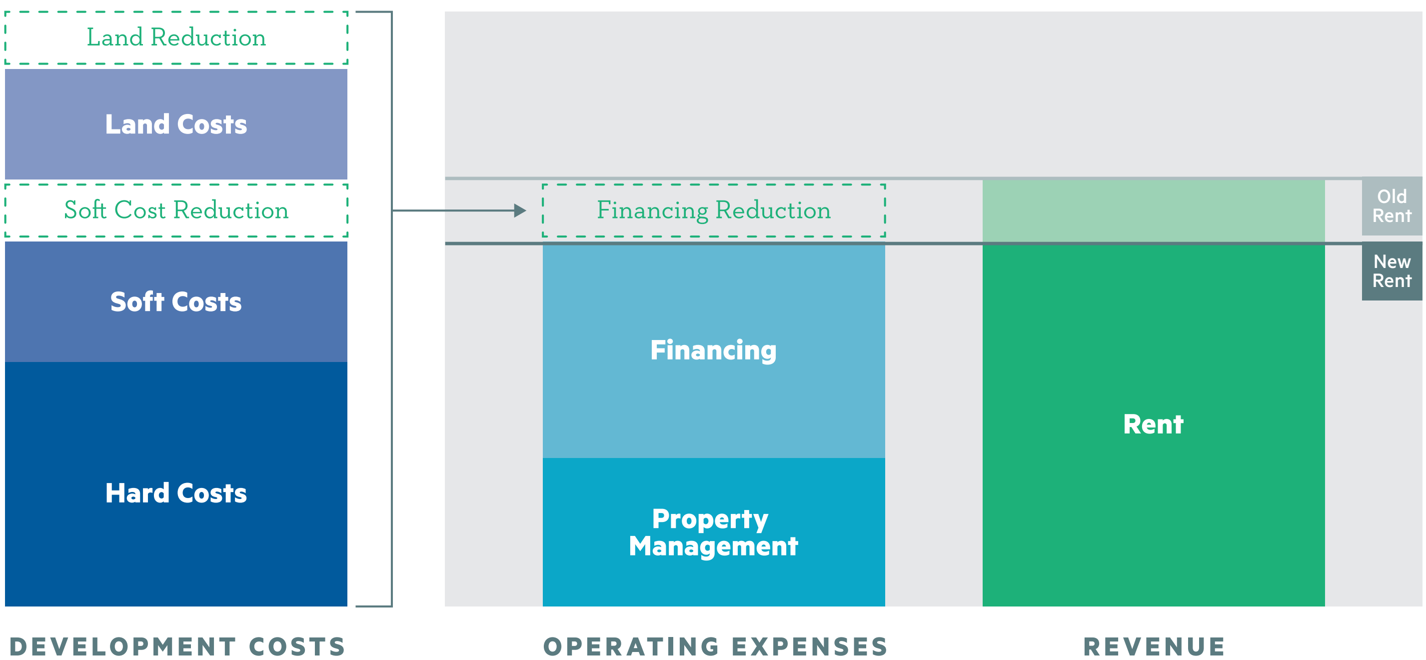
By-right development impacts affordability in two key ways – it reduces the cost of development and increases the supply of housing.

Reduced Development Costs

By-right development reduces both soft costs and land costs. An efficient and predictable entitlement process reduces carrying costs, consulting fees, and other costs associated with approval processes when compared to a lengthy discretionary review process. Land costs are reduced when the zoning premium on multifamily land is rendered obsolete – by-right policies increase the number of parcels with few zoning restrictions, reducing competition and associated land costs.

When costs decrease, developments require less financing and less rent to ensure project viability. Policy changes that allow for more by-right development can lead to lower rents for individual multifamily projects, resulting in lower overall rents.

The magnitude of land and soft cost savings depends on the specific market conditions of each city, in addition to the current permissiveness and duration of the entitlement process.



By-Right Development Economics

By-right development impacts affordability in two key ways – it reduces the cost of development and increases the supply.

Increased Supply

By-right development policies increase the housing supply and, consequently, housing affordability. One of the largest factors driving the national affordability crisis is rising rents in existing low-rent housing. Those rent increases are the result of failing to build enough multifamily housing to accommodate new renter households.

By-right development increases affordability indirectly. As supply increases, it reduces competition for existing housing and leads to lower rents. This indirect impact can be significant. Below is the estimated[1] impact of a 1% increase in housing supply on rents and the number of households that would be able to afford rental housing as a result.

	DECREASE IN SHARE OF UNITS <$800 SINCE 2000 (PERCENTAGE POINTS)	EFFECT OF 1% INCREASE IN SUPPLY	
		REDUCTION IN RENT	INCREASE IN AFFORDABILITY (BY HOUSEHOLDS)
Atlanta	15.7	0.63%	690
Sacramento	19.5	0.98%	720
Minneapolis	15.1	0.95%	780
Denver	20.9	0.98%	1,300
Pittsburgh	21.1	1.19%	730
San Antonio	19.3	0.82%	720
Seattle	14.5	1.02%	1,500
Tampa	26.8	1.00%	580

A **1% increase** in overall supply in Pittsburgh would add **1,200 units** to the market and reduce overall prices by **1.19%**. This would make Pittsburgh affordable to **730** additional households.[2]

1 A 2018 study by the Bay Area Council Economic Institute ("Solving the Housing Affordability Crisis") evaluated the effect of various housing policies based on the number of households for which housing would become affordable as a result of the policy, using a 30% housing-cost-burden assumption. The report evaluated the responsiveness of price to changing the supply through policy. Using a similar method, HR&A evaluated the number of households for which housing would become affordable, given a 1% increase in the overall supply of the eight case-study cities.

2 730 additional households would pass the threshold below 30% for affordability.

Tool: Inclusionary Zoning

THE HOUSING AFFORDABILITY TOOLKIT

Developed in Partnership with
HR&A Advisors

Inclusionary Zoning

Inclusionary zoning policies can increase affordability if they are flexible, properly structured with sufficient incentives, and limited to strong housing markets.

What Is Inclusionary Zoning?

Inclusionary zoning policies require new rental housing developments to include a certain percentage of apartments at below-market rents in order to be approved. In exchange for those affordable units, most policies offer incentives that offset the costs of lower rents.

Common Incentives

- Additional development density
- Reduced parking requirements
- Accelerated approval
- Tax abatements*
- Impact fee waivers
- Design flexibility
- By-right development*
- Public financing

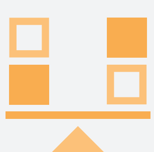
> **"Since 1974, almost 900 local governments have enacted inclusionary zoning policies, either mandatory or voluntary. Voluntary programs allow developers to determine whether market conditions are right for participation."**

How Inclusionary Zoning Works

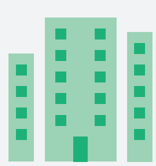
The economics of inclusionary zoning policies are often misunderstood. Inclusionary policies are viewed by many local governments as 'costless' solutions to their housing affordability challenges. **In reality, inclusionary policies impose significant costs on new rental development by reducing total rents on the property and making it harder for developers to get the financing they need to build.**

A well-designed inclusionary policy adheres to four principles that minimize and offset the costs the policy creates.

The Four Principles of Effective Policies



Provide a sufficient range of incentives to offset reduced rents



Target neighborhoods with strong housing markets

Provide developers with flexible participation options in housing markets

Enable simple administration and developer participation

*Additional information on these incentives is provided in subsequent tools documents.

Provide Sufficient Incentives

Without sufficient incentives, inclusionary zoning can actually reduce housing affordability.

If incentives do not cover the gap between the below-market rents and market-rate rents, owners will either have to raise the rents for the market-rate units or cancel plans to develop the property altogether. Both scenarios undermine affordability.

In markets where there is strong demand, the rents for market-rate units can rise to cover the reduction in rents on inclusionary units, shifting the cost of the reduced rent onto the market-rate units.

In markets where the demand for rental housing is not strong enough to support higher rents, projects on the margin may not be built. The decrease in development restricts supply and increases competition for existing housing, contributing to displacement and higher rents for existing rental housing.

Decreased Development Portland, OR

Since Portland's inclusionary policy took effect in February 2017, multifamily building permit applications have decreased 65%. The drop appears to be at least partially because the policy failed to provide sufficient incentives and created an onerous administrative process.

Source: Portland Housing Bureau

Even modest rent reductions not recovered through incentives significantly reduce the financing a property can secure. A $100 per month rent reduction for a single unit translates into approximately $20,000 less per unit in financing.

IMPACT OF RENT REDUCTION ON FINANCING

-$100 = -$20K

Reduction in Monthly Rent for 1 Unit = Financing Gap

The "cost" of an inclusionary policy to developers depends on how many below-market units are required and the allowable rent levels for those units. This example compares the burden of a policy that requires 15% of the units to be at 80% AMI* to a policy that requires 10% of the units to be at 60% AMI.

	Level of Affordability		# of units		Rent Reduction		Financing Gap
A	-$200 (80% AMI)	X	30	=	-$6K	=	-$1.2M
B	-$400 (60% AMI)	X	20	=	-$8K	=	-$1.6M

$100 reduction in monthly rent supports $20,000 in debt, assuming a 30-year amortizing mortgage with an interest rate of 5%.

AMI (Area Median Income) is a Department of Housing and Urban Development-determined measure of the household income for the middle household in a region.

Inclusionary zoning can also include for-sale homeownership housing. However, this is not addressed within this document.

Establishing Effective Incentives

Stakeholders should take a holistic approach when designing incentives.

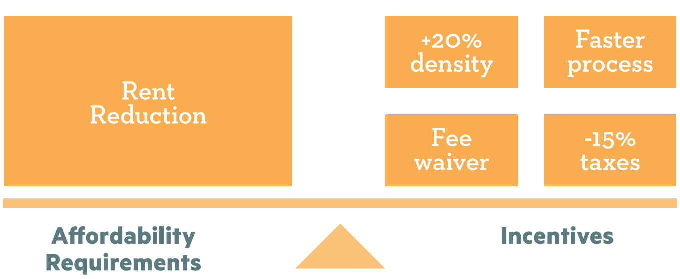
Collaborate with property managers, owners, and developers. Establishing a set of affordability requirements and offsetting incentives tailored to the conditions of a specific housing market is difficult absent input from stakeholders. These private sector partners are likely to have a more in-depth understanding of local market conditions from neighborhood to neighborhood and the complexities of multifamily housing finance than policymakers. Private sector partners substantive involvement in designing the program is necessary for its success. Since housing markets change over time, it may be necessary to engage them even after the policy has been adopted to modify it to adapt to changing market conditions.

Stakeholder Input Nashville, TN

In 2015, Nashville's Metro Planning Department convened stakeholders, including developers and lenders, to provide input on an inclusionary zoning policy through meetings and individual and group interviews. Their participation and input on land costs, development costs, rental rates and incentives helped develop a viable inclusionary policy that was adopted in 2016.

Possible incentives

- Additional development density "bonuses"
- Reduced parking requirements
- Accelerated approval
- Tax abatements
- Impact fee waivers
- Design flexibility
- By-right development
- Public financing

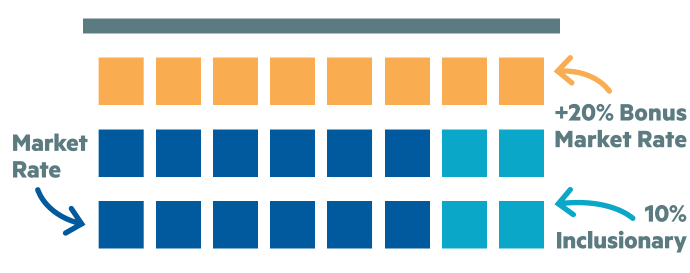


Policymakers need as many incentive options at their disposal as possible to accommodate the diversity of their housing market needs. Rarely will just one incentive program sufficiently offset reduced rent for every type of project and in every neighborhood. In some projects, additional density is more valuable in covering rent gaps than tax abatement. In other neighborhoods, the opposite may be true. Some developments may need to combine incentives to cover rent and financing gaps.

While density bonuses are the most common policy incentive used, they are not a panacea. Density bonuses are not always the most effective for many reasons.

1. They only work in a neighborhood where there is enough demand to absorb the additional units, otherwise there is no economic benefit to the bonus.
2. They only work if the extra density doesn't change the type of construction, such as going from a less expensive mid-rise building to a much more expensive high-rise property. In those cases, the increased construction costs will typically exceed the value of the density bonus.
3. The density bonus must allow for developers to add more market-rate units than the number of below-market rents required. A one-for-one incentive will not offset the reduced rent in an inclusionary unit.

DENSITY BONUS IN PRACTICE



Target Strong Markets

Effective inclusionary policies should target strong housing markets and vary according to market conditions.

> **"Areas not experiencing any or much market-rate development will likely not generate significant results from an IZ policy."**
>
> – Urban Land Institute

Inclusionary policies require strong housing markets to be effective. They depend on market-rate development to produce inclusionary units and demand from middle- and high- income renters to offset the reduced rent for inclusionary units. Neighborhoods with low rates of vacancy, high levels of construction, and steady growth in rent are most conducive to supporting an inclusive policy. Community perception about the strength of a real estate submarket often exceeds the actual strength of the market. A clear, data-driven assessment of the strength of the housing market is imperative for an informed discussion about where an inclusionary policy could be feasible.

Most cities do not have a strong enough housing market to support a citywide mandatory inclusionary policy. Many will have some neighborhoods with lower market rents, higher vacancies or limited development activity where incentives simply can't offset the cost of the below-market-rent inclusionary units.

Citywide inclusionary policies should include different incentives and requirements for different neighborhoods. A downtown housing market where large residential towers are being developed calls for a different policy than a former warehouse district where industrial buildings are being converted to loft apartments. Both might be strong markets, but the appropriate incentives and the number and kind of required below-market units will differ significantly. The inclusionary policy must be targeted accordingly to reflect these differences.

Inclusionary policies should be revaluated periodically. Since effective inclusionary programs require strong housing markets, inclusionary policies should be reviewed on a regular basis to determine if the incentives they offer still cover the rent gap in the current market conditions. Once again, engaging stakeholders, such as developers and property owners, is critical to ensure that the affordability requirements don't exacerbate housing affordability.

Regular Policy Updates Boston, MA

The City of Boston adopted an inclusionary zoning policy in 2000 that required any multifamily developer constructing 10 or more units, receiving funding from the city, developing property owned by the city, or receiving zoning flexibility from the city, to make 10% of the units affordable (or build the required units off site). In 2015, the city changed the on-site affordability requirements after a feasibility study and stakeholder input determined the current requirements were misaligned with market conditions. They began another policy review in March 2018.

Source: City of Boston, Boston Globe

Offer Flexibility

Effective inclusionary policies offer flexibility to developers in how they participate.

Mandatory inclusionary policies can harm affordability. If the policy does not offer sufficient incentives to cover rent gaps, developers will have to raise rents for the market-rate units or cancel plans to build. The opportunity for a mandatory inclusionary policy to harm housing affordability is significant because most are relatively complicated, apply across multiple neighborhoods and building types, and include a range of affordability requirements.

Voluntary policies are less risky for affordability. If the incentives in a voluntary program don't align with market conditions, developers can simply choose not to participate, but they can still build the housing the community needs. Assuming the policy is well-designed and incentives to include below-market-rent units outweigh the costs, developers will be motivated to participate.

Mandatory/Voluntary Mix New York, NY

NYC uses both mandatory and voluntary inclusionary policies in different areas of the city. The mandatory policy is closely linked to areas of the city where rezoning to allow for higher density is planned or has occurred. The voluntary program is used in neighborhoods that cannot support a mandatory policy.

Source: Housing Virginia, Fairfax County, VA

Engaging developers is the best way to ensure the best outcome for stakeholders and policymakers. Attracting sufficient participation can be a challenge with any inclusionary policy. As previously noted, if a mandatory policy doesn't offset the program costs, developers will build elsewhere. If the program is voluntary, they will opt out. Working with developers to design policies is one way to ensure they will be effective.

Voluntary Policy Fairfax County, VA

Fairfax County's Workforce Dwelling Unit (WDU) Program incentivizes development in high-density areas. If developers choose to opt-in to providing affordable workforce units within their high-rise developments, they are granted an up to 20% density bonus. Since these buildings are already employing higher-cost construction, the bonus has real economic value. In addition, the policy targets households at higher incomes, those earning between 60% and 120% of AMI, which reduces the rent gap between the market-rate and workforce units. Twenty-five include units that participate in the WDU program, creating approximately 1,200 units for workforce renters.

Source: Housing Virginia, Fairfax County, VA

Include a payment in-lieu option. Many inclusionary policies allow developers to pay a fee to the jurisdiction in-lieu of including below-market units in their development. These set fees reduce risk to the developer and encourage their participation in the program. Under them, they know they won't face unexpected costs from delays in finding a qualified resident, ongoing monitoring requirements, or other additional requirements.

The developer can weigh the cost of the fee in-lieu against the incentives the policy offers and make a choice about whether and how to participate. If the policy is mandatory, the fee still eliminates the administrative burden and risks of participation. Localities can use these fees to provide grants to nonprofits to build affordable housing where it is needed most and may be more cost effective to produce.

Keep It Simple

Inclusionary policies that are simple to comply with are more effective.

Administratively complex programs harm affordability. They take more time and resources with which to comply, which increases their "costs" to developers and results in higher rents or fewer units being developed if developers opt out.

Keep income documentation and reporting requirements simple. Don't default to burdensome federal requirements. Federally funded affordability programs are overly complex and discourage private sector participation as a result. Many local inclusionary policies default to burdensome federal rules for income documentation and recertification because they think it is easier for their local housing departments to administer. That simplicity comes at a cost to developers in terms of training and compliance, which affects their decision on whether or not to participate in a voluntary inclusionary program or whether or not to build in a jurisdiction where it's mandatory.

Annual Reporting Montgomery County, MD

Every April, property owners must report the number of below-market units leased, residents' names, household size, dates of lease and lease expiration, total annual household income and a notarized statement that the residents meet the eligibility requirements to the best of the property owner's information. These requirements exemplify a streamlined process, breaking from more onerous federal requirements.

Source: Montgomery County, MD

Ensure the resident selection process does not make it difficult to lease inclusionary units. Identifying residents eligible to occupy the inclusionary units can add significant costs to owners and can delay filling a building if they are unable to find residents. To avoid this, resident screening requirements should be clear and easy to incorporate into the standard screening process. One best practice to reduce the costs of delay is for local governments to work with a nonprofit partner to identify a pool of eligible residents from which property owners can draw.

Inclusionary policies should maximize production by focusing on unit sizes and bedrooms, not finishes and materials. The size of a unit and the number of bedrooms are directly related to affordability, and an inclusionary policy can reasonably require that inclusionary units be comparable to market-rate units to maximize production. An effective inclusionary policy does not establish requirements about materials, location within the building, and access to amenities for inclusionary units. These are not issues related to affordability and can decrease the number of units a developer is able to deliver.

Resident Selection Montgomery County, MD

Basic resident eligibility requirements include gross income requirements, primary residency status, and not having owned residential property within the past five years. Prospective residents must complete a certification form and submit most recent federal tax returns, W-2s and pay stubs. Similar to annual reporting, these requirements are streamlined and do not default to more extensive federal requirements.

Source: Montgomery County, MD

Considerations & Limitations

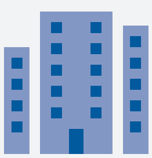
Before deciding to pursue an inclusionary housing policy, local governments should consider the limitations and benefits.

It can be very difficult to get an inclusionary zoning policy right. As this document explains, if the locality doesn't include the right incentives to offset the cost to comply with these programs, they can actually worsen their affordability challenges.

Local governments and the communities they serve should also have **realistic expectations about the number of inclusionary units and the level of affordability a policy will achieve.** The number of units produced by inclusionary policies is typically a small percentage of development in the area subject to the policy.

Few policies are effectively able to serve extremely low-income households because of the deep subsidy level required. **An inclusionary policy can be an effective component of a larger affordability strategy, but it will not be sufficient to address all affordability challenges of any community alone.**

Housing Goals



UNITS PRICED AFFORDABLY

MIXED-INCOME NEIGHBORHOODS

In implementing housing policies, local governments may pursue a range of housing goals. Properly structured inclusionary policies can be effective at **creating units with affordable rents and mixed-income neighborhoods,** but will not necessarily address racial segregation, displacement of existing residents, or other housing goals.

Impact

> **"Average annual production under local IZ programs varies across regions, but in all areas has contributed only a modest amount of affordable housing."**
>
> – Lance Freeman, Columbia University and Jenny Schuetz, Federal Reserve System

1 The White House (Obama Administration) Housing Affordability Toolkit, September 2016

Recommendations

To design an effective inclusionary policy, a city should take a four-tiered approach.

PROVIDE SUFFICIENT INCENTIVES: WITHOUT EFFICIENT INCENTIVES, INCLUSIONARY ZONING POLICIES CAN ACTUALLY REDUCE HOUSING AFFORDABILITY

- If incentives do not cover the gap between the below-market rents and market-rate rents, owners will either have to raise the rents for the market-rate units or cancel plans to develop the property altogether.
- Even modest rent reductions not recovered through incentives significantly reduce the financing a property can secure.
- The "cost" of an inclusionary policy to developers depends on how many below-market units are required and the allowable rent levels for those units.
- Collaborate with property managers, owners, and developers.
- Policymakers need as many incentive options at their disposal as possible to accommodate the diversity of their housing market needs.
- While density bonuses are the most common policy incentive used, they are not a panacea.

TARGET STRONG MARKETS: EFFECTIVE INCLUSIONARY POLICIES SHOULD TARGET STRONG HOUSING MARKETS AND VARY ACCORDING TO MARKET CONDITIONS

- "Areas not experiencing any or much market-rate development will likely not generate significant results from an IZ policy" – Urban Land Institute.
- Most cities do not have a strong enough housing market to support a citywide mandatory inclusionary policy.
- Citywide inclusionary policies should include different incentives and requirements for different neighborhoods.
- Inclusionary policies should be revaluated periodically.

OFFER FLEXIBILITY: EFFECTIVE INCLUSIONARY POLICIES OFFER FLEXIBILITY TO DEVELOPERS IN HOW THEY PARTICIPATE

- Mandatory inclusionary policies can harm affordability.
- Voluntary policies are less risky for affordability.
- Engaging developers is the best way to ensure the best outcome for stakeholders and policymakers.
- Include a payment in-lieu option.

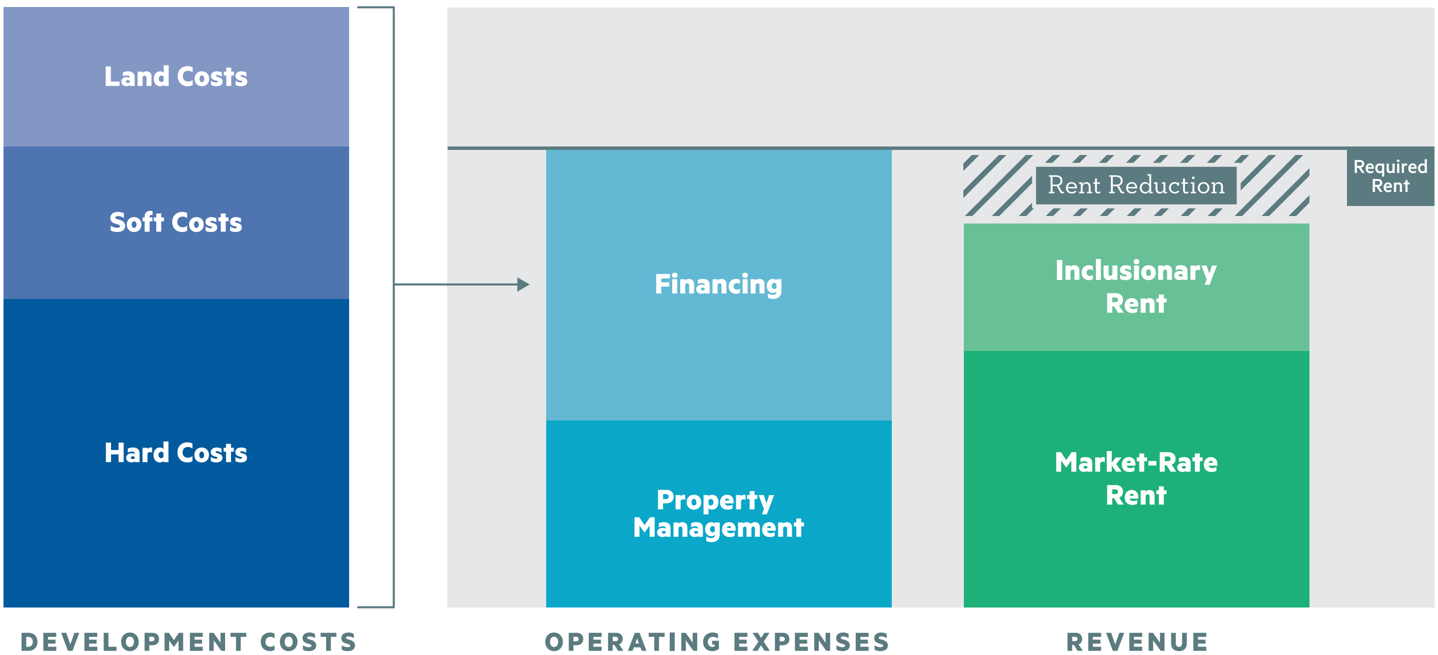
KEEP IT SIMPLE: INCLUSIONARY POLICIES THAT ARE SIMPLE TO COMPLY WITH ARE MORE EFFECTIVE

- Administratively complex programs harm affordability.
- Keep income documentation and reporting requirements simple. Don't default to burdensome federal requirements.
- Ensure the resident selection process does not make it difficult to lease inclusionary units.
- Inclusionary policies should maximize production by focusing on unit sizes and bedrooms, not finishes and materials.

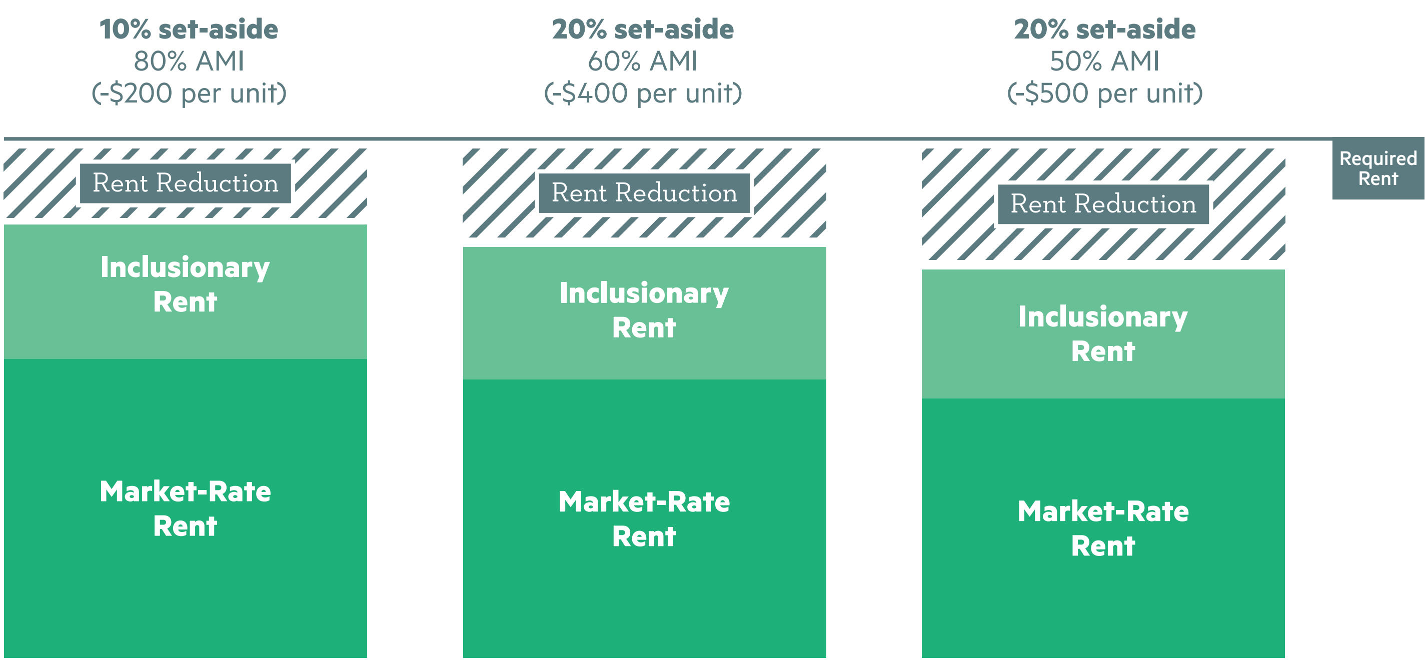
Economics of the Tool

Revenue from rent is reduced as affordability requirements are added.

The addition of inclusionary units in a new development introduces a gap in revenue. Without adequate revenue to cover expenses, a project becomes infeasible.



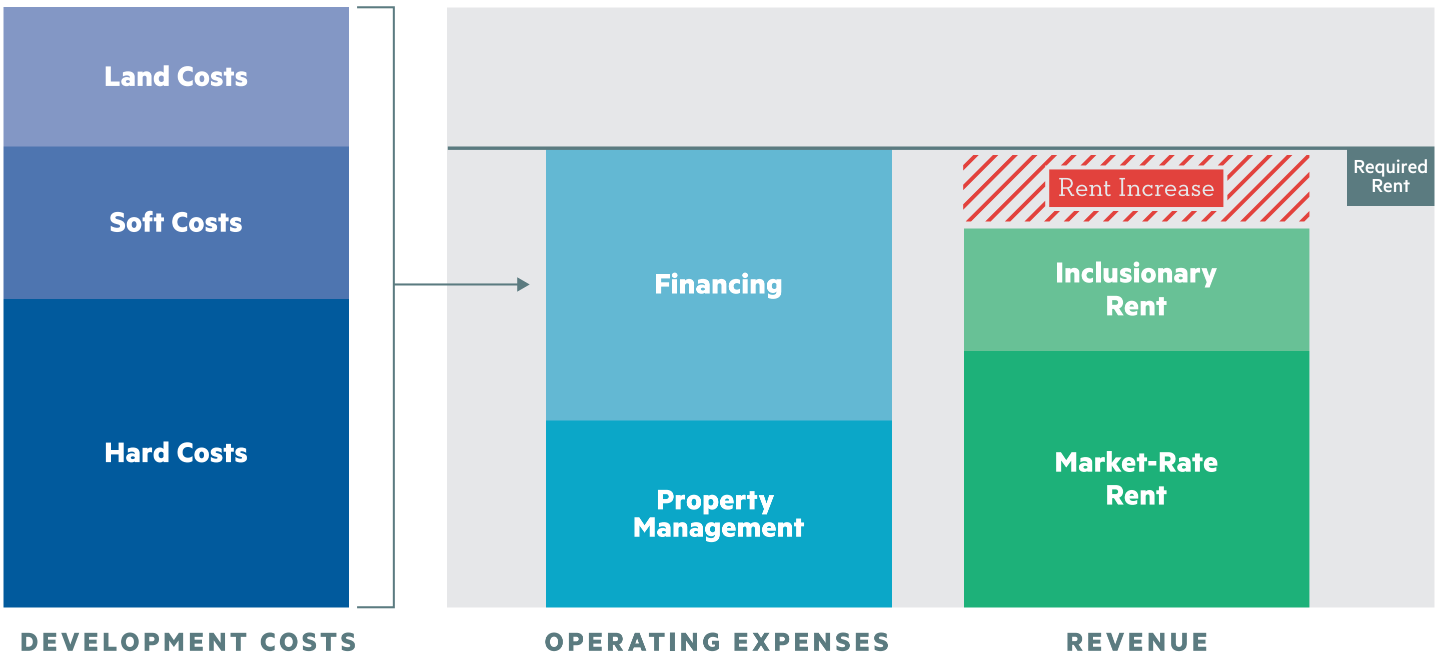
As affordability requirements deepen, the reduction in rent expands.



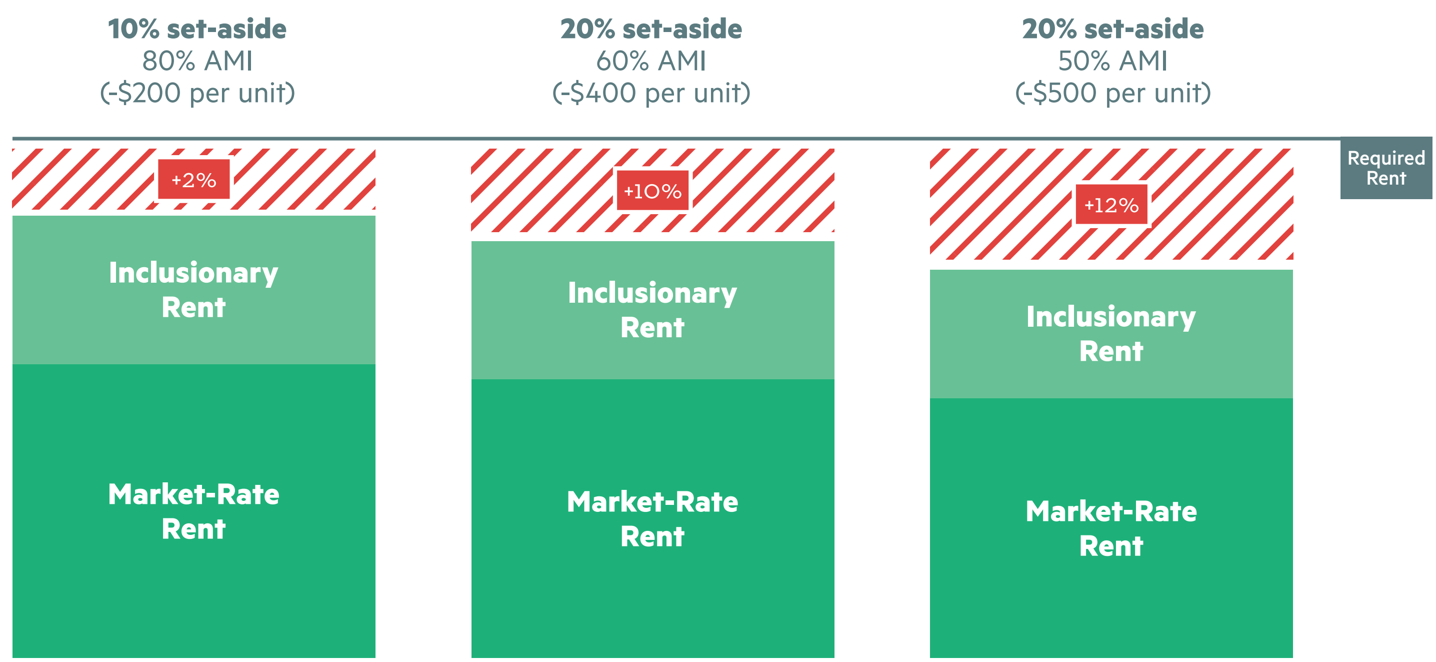
Economics of the Tool

Without incentives, market-rate rents must rise to offset the reduction in rent for inclusionary units.

Market-rate rents rise to cover the gap in revenue created by the affordability requirements.



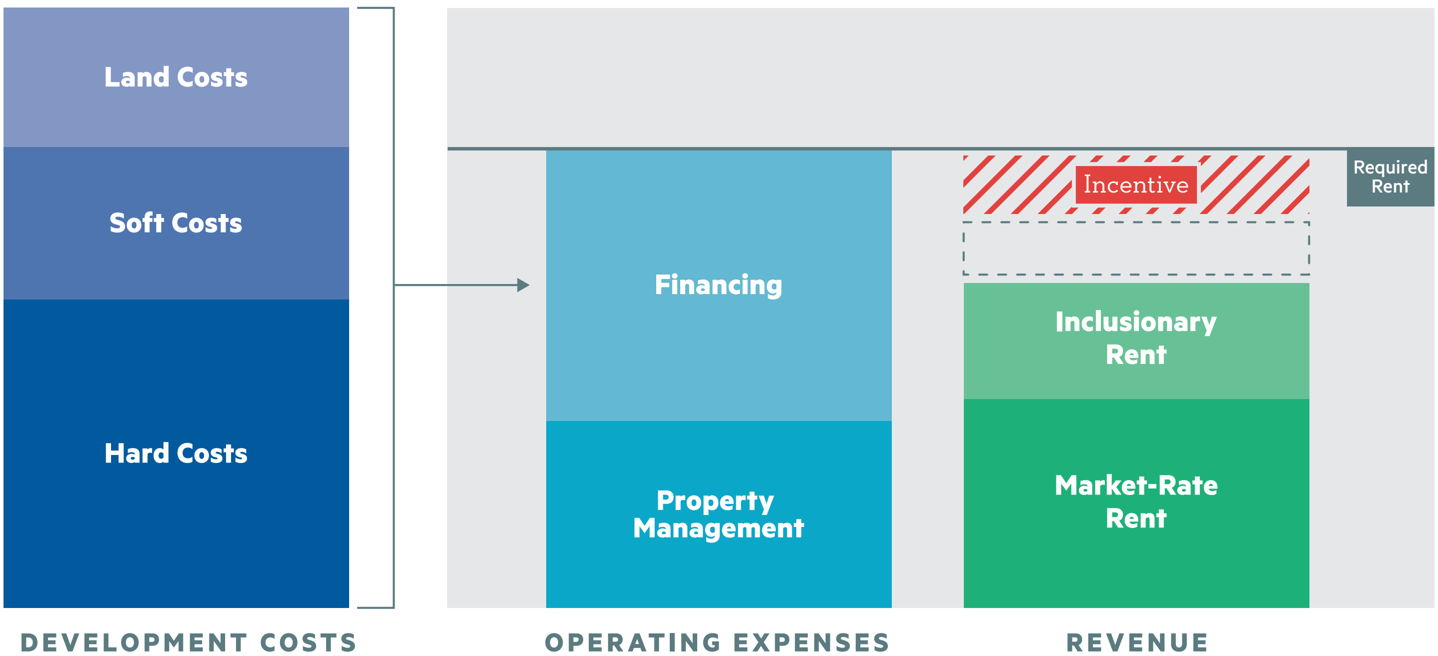
As affordability requirements deepen, the required rise in rent grows. If the market cannot support the increase, the project will not be built.



Economics of the Tool

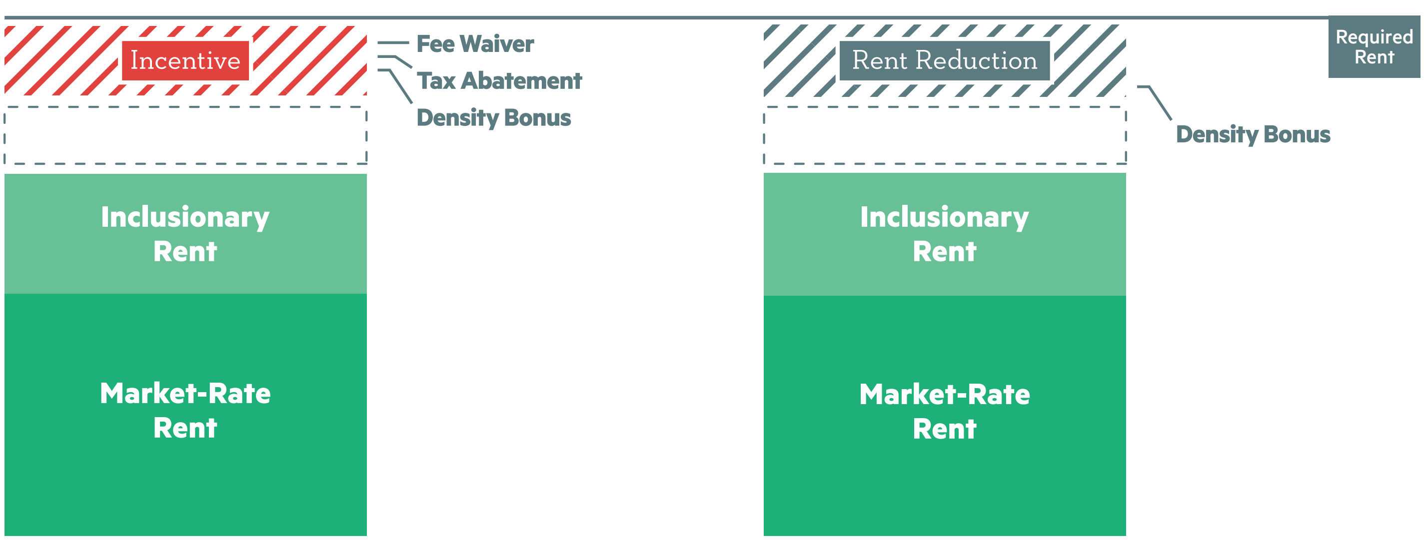
Incentives can offset the reduction in rents from inclusionary requirements.

Jurisdictions can offer a variety of incentives to close the revenue gap. The incentives can lower development costs or operating expenses or increase the revenue earned from market-rate development.



If an incentive package addresses the gap created from rent reduction, market-rate rents will not rise.

If the incentives do not sufficiently fill the gap, market-rate rents will still rise, but to a lesser degree.



NATIONAL
MULTIFAMILY
HOUSING
COUNCIL

Tool: Public Land Economics

THE HOUSING AFFORDABILITY TOOLKIT

Developed in Partnership with
HR&A Advisors

Public Land Policy

Selling public land at a below-market price to subsidize the development of housing can improve affordability in a community.

What Is a Public Land Policy?

A public land policy for affordable housing is a process and set of criteria established by a local government to select and sell parcels of publicly controlled land at below-market prices (often free) to improve affordability. The reduced land price lowers the cost of development and allows for lower rents and greater affordability.

Public land includes any land that is owned or controlled by a government entity or quasi-governmental entity, including:

- Transit agencies
- Housing authorities
- Redevelopment agencies
- Municipal facilities
- School districts

> **"Allocating public land for affordable housing can be an especially valuable way to reduce development costs and meet housing needs with less need for public subsidy."**
>
> – Urban Land Institute

How Public Land Policies Work

The sale of public land involves a public-private partnership between the government entity that controls the land and the private developer who creates the housing. Public land sales typically follow these steps:

1. Selection of a parcel of public land

2. Land listed for sale

3. Proposal or bid submission

4. Public-private partnership established

5. Development

Effective Public Land Policies

A well-designed public land policy will adhere to the three principles below to maximize value and community benefit.

1. Include a broad portfolio of publicly controlled land.

2. Maximize the value of public land.

3. Ensure a defined selection process.

Considerations

Before adopting a public land policy, local governments should consider how it fits in a larger housing affordability strategy.

Impact

The impact of public land disposition is directly tied to the **quantity and quality of land made available for development. More and better quality parcels can have a greater impact on affordability.**

In most communities, a public land disposition policy alone, even with a significant portfolio, will produce less than 100 units annually. As such, public land disposition should complement a larger housing affordability strategy and is not a solution on its own.

Market

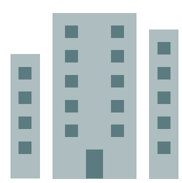
Public land disposition can operate effectively and create community benefits in strong and weak markets alike. In strong markets, disposition creates opportunities for affordably priced housing where market forces would otherwise price out affordable units. In weaker markets, discounted land values create an opportunity to catalyze reinvestment while maintaining the affordability of the neighborhood.

> **“In a constrained financial environment, [public land] can be an asset, regardless of market strength."**
>
> – Enterprise Community Partners

Prioritizing Tax Credit-eligible Parcels in Wake County, NC

Wake County reviewed its portfolio of publicly owned land, prioritized land that was likely to leverage LIHTC projects. By leveraging LIHTC, and other funding sources, Wake County increases the impact on affordability of selling public land at below-market prices.

Housing Goals



UNITS PRICED AFFORDABLY

MIXED-INCOME NEIGHBORHOODS

In implementing housing policies, local governments may pursue a range of housing goals. Public land disposition policies are effective at **creating units with affordable rents, as well as promoting mixed-income neighborhoods.** However, public land disposition policies do not address displacement or preservation of existing housing.

Recommendations

1. Effective public land policies include a broad portfolio of publicly controlled land.

Conduct a thorough inventory of public land before adopting a public land policy. Local officials need to understand what parcels are available, any barriers to developing them as housing, and scale of housing they will produce to make their policy effective.

Apply public land policies to land held by all governmental departments and quasi-governmental agencies. Policies limited to a single department or direct control by local government are less effective. Instead, local governments should consider not only land they control directly, but also land controlled by their public partners to ensure they also prioritize housing affordability when making disposition decisions.

Local governments should look to include land controlled by:

- Transit agencies
- Housing authorities
- Redevelopment agencies
- Municipal utilities
- School districts

Prioritize high-value sites. There is often pressure to exclude high-value sites because selling those parcels at a reduced price has a greater impact on a local government's budget. However, including these sites allows localities to increase affordability in more desirable, high-opportunity neighborhoods that are often closer to jobs and transit. It also fosters mixed income communities.

Encourage co-location of government facilities and housing. Many communities limit public land policies to 'surplus land', which only includes vacant and unused parcels. This narrow definition covers only a sliver of public land in most communities. A more expansive view that includes parcels with existing government facilities on them broadens the portfolio of available land to help housing affordability.

Redesign public facilities to support co-location. Redesigning public facilities to support co-location with housing is difficult. It often involves higher construction costs and scrapping existing design standards. However, it is necessary to expand the portfolio of public land and have an effective public land policy. Large surface parking lots can be an opportunity to co-locate housing with existing facilities. For new development, facilities will have to be redesigned, such as shifting an elementary school from one to three

Fire Station Co-location

In Washington, DC's Foggy Bottom neighborhood, the city used a competitive solicitation process for two District-owned parcels to create a fire station that included 52 units of affordable housing above it. The result is *West End Square 50*, a 110,000 square foot, mixed-income, multi-use development.

> **"Thinking outside of the box resulted in a project that is putting residents into high-quality homes that are close to amenities, transit, and crucial safety services like this new fire station."**
>
> – Polly Donaldson, Director of Housing and Community Development, D.C. Government

Recommendations

2. Effective public land policies maximize land value, contributing the value in exchange for greater affordability.

The more land value contributed to a project, the greater the affordability that can be obtained. Local governments should consider contributing land for free or at the greatest possible discount to maximize affordability.

A public land policy should allow for mixed-income developments. Mixed-income housing developments have greater value and can provide more subsidy to improve affordability. The value from rents for market-rate units can be used to offset the reduced rent for affordably priced units, allowing for deeper affordability, or more units with affordable rents. Public land can be used to model and catalyze the type of mixed-income development a local government wishes to see more of in the market. *See the public land tool for a more detailed description of how mixed-income development increases affordability.*

High-Density Transit-Oriented Workforce Housing in Atlanta, GA

Atlanta's public land disposition guidelines, which include zoning relief for project modifications, and higher density uses and reduced parking requirements, helped the Metropolitan Atlanta Rapid Transit Authority (MARTA) recruit developers for station-area transit-oriented demand (TOD) contracts that include workforce units.

> **"...public land can play an important role in providing the diversity of housing the city needs, especially in areas with high and rising values."**
>
> – Coalition for Smarter Growth

A local government should use its regulatory authority to allow for higher density development. Local governments are better positioned to obtain approval for higher density development than private developers. By securing the ability to develop at a higher density prior to disposition, the local government increases the amount of housing that will be developed and the value of the land that can be used to support affordability.

Public land used to improve housing affordability should be "fast tracked" through regulatory approval processes. A streamlined or "fast tracked" regulatory approvals process encourages developers to make proposals for the development of public land and speeds up the process of housing being brought online. This is another area where local governments can increase the value of the land, and thus the subsidy available to support affordability.

Recommendations

3. Effective public land policies follow a defined selection process.

Local governments must use a clear and simple selection process. Overly complex selection processes discourage developer participation out of concerns that the final selection will be subjective or influenced by factors other than strength of their proposal. A simple and clear process will attract more, and stronger, developer responses, which will ensure the local government is getting the most public good in exchange for the discounted land value.

Community Engagement: Baltimore, MD

Community engagement is a key part of Baltimore's "21st Century Schools Initiative," in which Baltimore City Schools will transfer 26 school buildings to the City over a 10-year period.

The City created a robust community engagement process to explore opportunities to re-use and redevelop the schools. It included a dedicated website with an explanation of the redevelopment process, a detailed map and inventory of properties, and an opportunity to submit an expression of interest in school re-use or redevelopment.

Affordability goals and public benefits should be defined in the solicitation. Affordability goals might be tied to the number of units, income levels, or tenure type. Public benefits could include park space, infrastructure improvements, or community facilities. Local governments should make their goals clear so developers can focus their proposals on the desired public objectives and local officials can evaluate and defend strong proposals.

Affordability Goals: Transit in Seattle, WA

Seattle's metropolitan transit agency, Sound Transit, introduced an "equitable transit-oriented development" policy for land disposition. The policy designates surplus properties for the development of affordable units, following voter-approved transit investments.

The agency requires that developers set aside 80 percent of their residential units for tenants earning 80 percent of the area median income or below. Designated surplus properties now have upwards of 600 units planned for development throughout the Seattle metropolitan area.

Community engagement should be carefully incorporated into a public land policy. To ensure community support for redevelopment, engagement must be initiated early on. Understanding neighborhood expectations at the outset can prevent eventual opposition to development that slows the building development and production of affordably priced units.

Public Land Policy

Effective public land policies follow a defined selection process.

Five-Step Framework for Public Land Disposition

As local governments develop their public land policy, they should adapt a basic framework to meet their needs. It is important to adopt a clear process, enabling local governments to work through an entire portfolio of publicly held land and ensure the greatest impact possible. Without a clear implementation process, a local government is likely to approach each parcel of land on a one-off basis and never work through its entire portfolio, greatly limiting opportunities for affordability.

1. Selection of a Parcel of Public Land

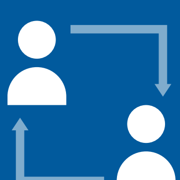
An inventory of public land is conducted to evaluate the suitability of publicly controlled land for housing development. One or more feasible sites are then selected to list for sale.

2. Land Listed for Sale

Local government issues a request for proposals (or bids) to develop the housing. Land may be listed with specific housing requirements or with defined criteria on which proposals compete.

3. Proposal or Bid Submission

Interested developers submit proposals or bids that are reviewed and scored by the local government.



4. Public-Private Partnership Established

Local government selects a developer and negotiates a development contract with them, entering into a public-private partnership.

5. Development

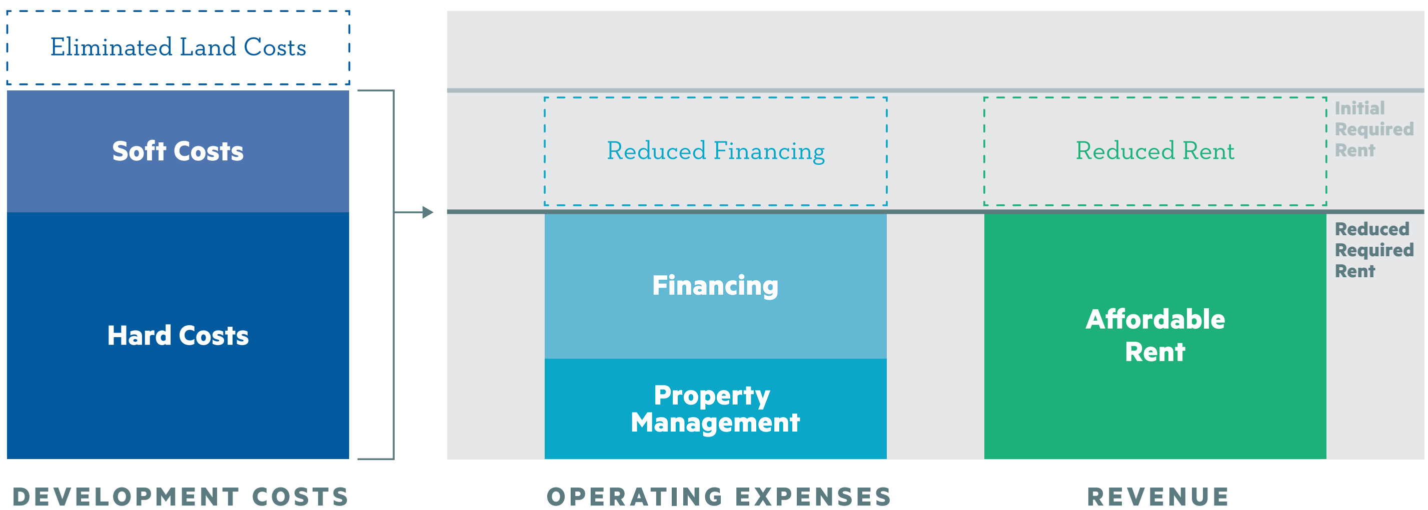
The selected developer executes the development and the proposed housing is built, improving affordability in the community.

Public Land Economics

The subsidy from the discounted sale of public land can either be spread across all of the units built or concentrated in a few.

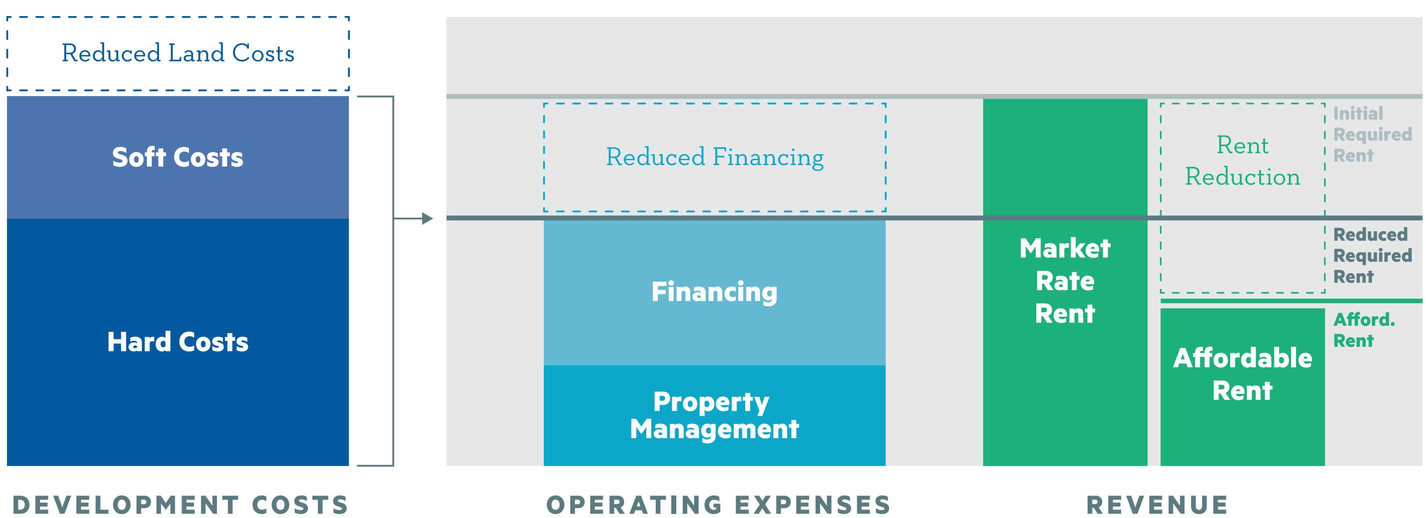
Fully Affordable Developments

A requirement that 100% of the units be affordable creates more units with below-market rents but lowers the rents by a smaller amount. To reach rents that are affordable to households with low incomes, other housing tools, such as tax abatement or public financing (Low-Income Housing Tax Credits, etc.), should be combined with the discounted sale of public land.



Mixed-Income Developments

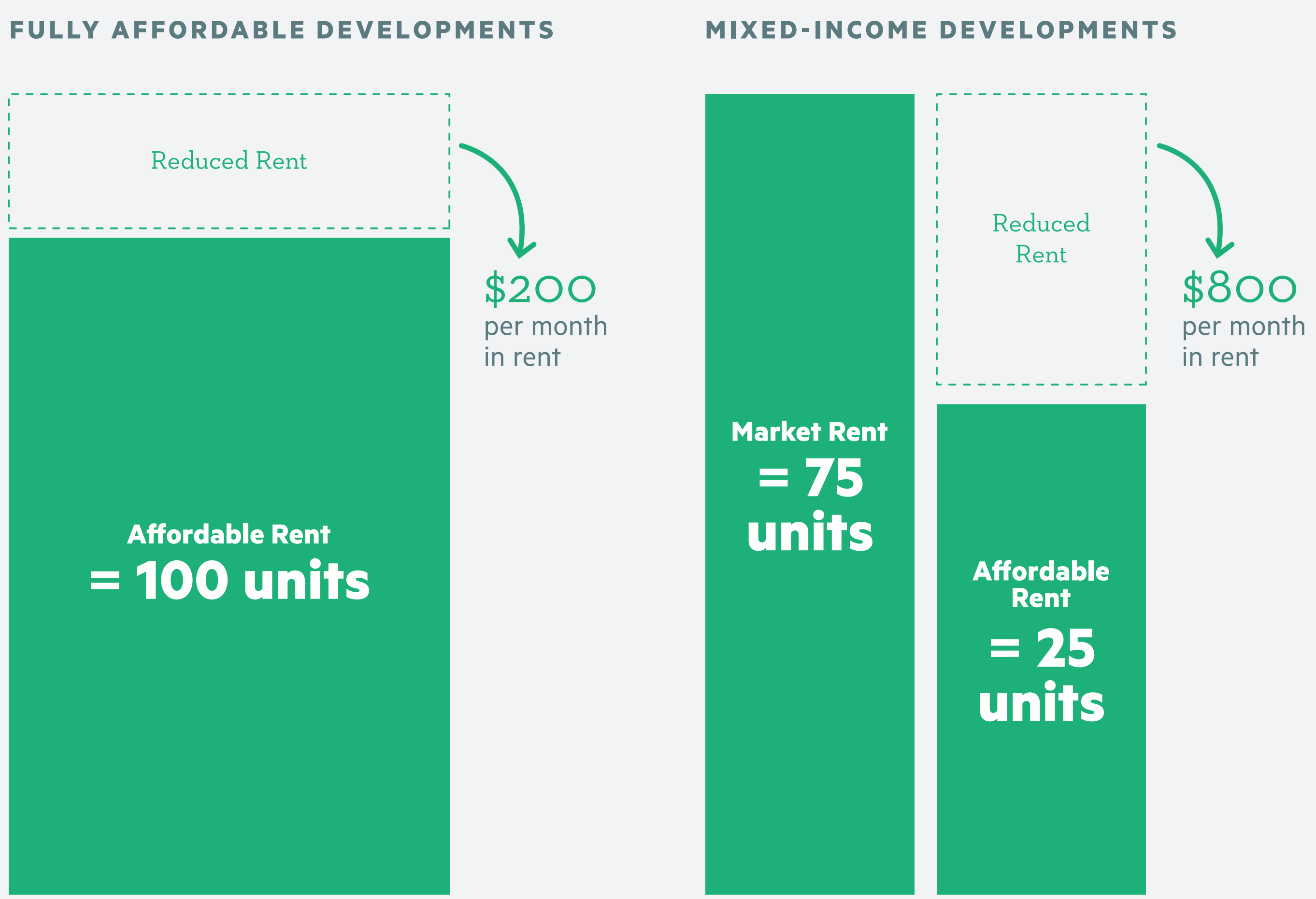
If a public land policy allows for mixed-income development, the subsidy from the discounted land can be targeted to fewer units, and those units can have significantly lower rents. The fewer the units with below-market rents, the greater the discount.



Public Land Economics

Public land policies should be crafted to target development projects that will advance community goals.

Local entities should have clear priorities when developing and executing a public land policy. If the goal of the policy is to moderately reduce rents for as many households as possible, then public land should be targeted toward fully affordable developments. If the goal is to significantly reduce rents for a smaller group of severely burdened households, then public land should be used for mixed-income developments.



FULLY AFFORDABLE DEVELOPMENTS

- **Small reduction in rent ($200) for all units**
- **100 units with reduced rents**

MIXED-INCOME DEVELOPMENTS

- **Deep reduction in rent ($800) for 25 units**
- **75 units with market rents**

Recommendations Summary

To design an effective public land policy, a city should take a three-tiered approach.

1. EFFECTIVE PUBLIC LAND POLICIES INCLUDE A BROAD PORTFOLIO OF PUBLICLY CONTROLLED LAND

- Apply a public land policy to land held by all governmental departments and quasi-governmental agencies (e.g., transit or redevelopment agencies, housing authorities, municipal utilities, school districts, etc.)
- Prioritize high-value sites, rather than exempting sites in desirable areas.
- Encourage co-location of housing and government facilities, including redesigning public facilities.
- Conduct a thorough inventory of land to understand availability and barriers.

2. EFFECTIVE PUBLIC LAND POLICIES MAXIMIZE LAND VALUE IN ORDER TO CREATE MORE AFFORDABLY PRICED UNITS

- The more land value contributed to a project, the greater the affordability.
- By allowing mixed-income, high-density developments on high-value sites, public land policies can create more affordability.
- Public land can be used to model and catalyze the type of mixed income development a local government wishes to see more of in the market.
- Affordability can also be supported through ‘fast tracked’ regulatory processes, reducing uncertainty and development costs that threaten affordability.

3. EFFECTIVE PUBLIC LAND POLICIES FOLLOW A DEFINED SELECTION PROCESS

- The best selection processes will be clear and simple enough to attract a broad range of developers and competitive proposals, ensuring that a local government can get the best possible public value from a discounted land sale.
- Public benefits and affordability goals must be detailed and specific, helping developers strengthen their proposals.
- Early and effective community engagement is critical to a successful public land policy. Engagement can help to create a broadly supported selection criteria and prevent eventual community opposition to development.

NATIONAL MULTIFAMILY HOUSING COUNCIL

Tool:
Tax Abatement

THE HOUSING AFFORDABILITY TOOLKIT

Developed in Partnership with
HR&A Advisors

Property Tax Incentives

Property tax incentives improve affordability by directly lowering rents or increasing the supply of rental housing.

What Are Property Tax Incentives?

Property tax incentives are state or local policies designed to reduce the tax burden on properties in order to support a public policy goal. The specific mechanisms vary by state and local municipality, but often fall under three broad categories: **tax abatements, tax rebates, and tax exemptions**. All three mechanisms have similar results – a net reduction in property taxes paid and lower operating costs.

TAX ABATEMENTS

Direct reduction in the amount of taxes owed.

TAX REBATES

A reduction in taxes applied after taxes are paid.

TAX EXEMPTIONS

A reduction in the appraised value of a property – thereby reducing overall taxes owed.

> **"Tax incentives can enhance development feasibility by allowing operators to reduce their operating costs."**
>
> – Urban Land Institute

How Tax Incentives Work

Tax incentives can work in two ways – a direct approach that provides incentives in exchange for rents at a certain affordability level and a supply approach that focuses on increasing the overall supply of rental housing to reduce the demand pressure on existing units.

DIRECT APPROACH

A well-run direct incentive program can increase affordability by requiring a reduction in rent in exchange for a commensurate reduction in property taxes. These incentives can be achieved either through negotiations between the developer and the municipality or through established government programs.

SUPPLY APPROACH

A well-run supply incentive program focuses on increasing the overall supply of housing by providing an incentive for an overall property, which would reduce the market rents required for new development and make more development feasible. Increased supply in a market can stabilize or reduce rents and decrease the likelihood that existing residents are displaced.

Effective Policies:

1. Define a clear and feasible approach

2. Balance affordability requirements with incentives

3. Enable simple administration and developer participation

Considerations

Tax incentives are flexible tools that can be adapted to support affordability.

Impact

Tax incentive policies vary greatly depending on how they are structured and targeted. It is important to ensure that the units developed due to an incentive would not have been built otherwise. This is typically referred to as a “but for” test and is an important analysis to ensure that limited public resources are used effectively.

DIRECT APPROACH

A direct approach functions as an operating subsidy – each dollar of tax abatement provided can result in an additional dollar of affordability per unit. This is an expensive option for municipalities, especially in areas with a substantial number of lower-income households where there is a large gap between what households can afford and the rent required to build and operate the unit. In these cases, a direct approach is most effective when complemented by other sources of subsidy.

SUPPLY APPROACH

A supply approach has an indirect impact on affordability by increasing the overall supply of housing through incentivizing a developer to build by removing the tax liabilities for a set period on an entire property. The new market-rate units help prevent rents in existing properties from rising. Depending on a jurisdiction’s existing market conditions, the impact of increased supply on affordability can be substantial.

Market

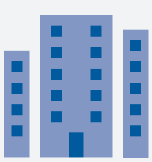
DIRECT APPROACH

A direct approach can work in any market. Municipalities need to decide if the net benefit of an incentive outweighs the cost of the foregone revenue.

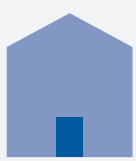
SUPPLY APPROACH

A supply approach is more effective in a weaker market where rents do not support new construction. Providing tax incentives reduces the amount of financing a project would require, lowering required rents.

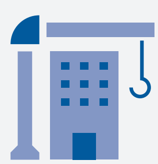
Housing Goals



UNITS PRICED AFFORDABLY



AVOIDING DISPLACEMENT



INCREASING QUALITY OF HOUSING STOCK

MIXED-INCOME NEIGHBORHOODS

Tax incentives are a flexible tool and can help meet a variety of policy goals. Carefully targeted requirements and policy design are key to ensuring that tax incentives work effectively.

Recommendations

1. Effective tax incentives have a defined and feasible approach to increase affordability.

Tax incentive policies should not only be limited to units that receive other federal and state subsidy sources. Combining tax incentive policies with other public funding sources like discounted loans, federal funding, or a local housing trust fund can leverage funding and allow a local government to set rents that are affordable for households with very low incomes. However, allowing apartments that are not receiving other public funding to access tax incentives expands the number of units that are available at below market rents. These tax incentives may be targeted toward middle-income households.

Tax incentives should be geographically targeted based on market conditions. Like other affordability tools, tax incentives should be responsive and adaptive to the market. Incentives that require high levels of affordability will not be effective in weaker markets, while there is a risk of over-subsidizing low levels of affordability in stronger markets.

Using incentives to drive investment in Philadelphia, PA

Philadelphia's tax incentive policy is designed to induce development by applying a 10-year tax incentive to address weak market conditions coupled with the fourth-highest construction costs in the country.[1] The program started in 2000 and applies across both rental and for-sale communities. Development increased by 376% in Philadelphia since the incentive took effect,[2] while Philadelphia suburbs without the incentive saw an 11% decrease in building activity. A report by JLL found that every $1 in tax revenue foregone through initially abated property results in $2 of net revenue through the resultant effects of the policy.

Philadelphia's program offers a blueprint for relatively weak-market cities looking to boost development and increase housing supply.

The flexibility of tax incentives should be used to create an approach customized to a market. In markets where the supply of housing is limited by a lack of developable land, a direct approach is best. However, a supply-based approach may be most effective in markets where housing is not being created for middle-income renters because prevailing market rents cannot support development costs. In these cases, an operating subsidy reduces the rent required for a project to be feasible and supports new production.

Tax Incentive "tiers" in Jersey City, NJ

Jersey City, NJ has had a development boom since 2000. However, growth has been uneven – neighborhoods with existing transit have developed the most, while others are still losing residents.

In response, the City enacted a tiered tax incentive in 2013 that grouped neighborhoods into four tiers, based on prior development activity. Tier 1, with the most development, has a tax incentive term of 10 years and 10% set-aside for affordable housing. Tier 4 neighborhoods have a tax incentive term of 30 years with 15% set-aside for affordable housing to protect existing residents. This program is designed to allocate tax-incentive dollars to maximize development and equitably distribute affordable and market-rate housing.[3]

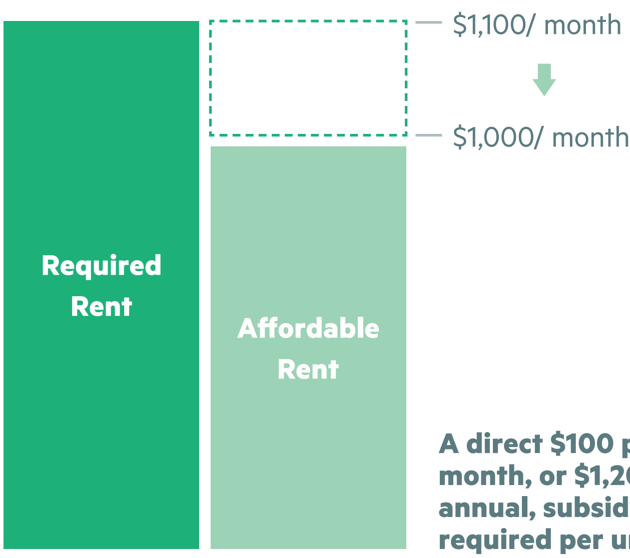
1 ENR.com
2 BIA Building Industry Association, 2017
3 Misra, Tanvi. Citylab, 2015

Recommendations

2. Effective property tax incentives are balanced with affordability requirements.

Successful tax incentives can have economic, fiscal, and policy benefits that outweigh the implementation costs and foregone tax revenue. Property tax incentives should be considered like other economic development-focused tax incentives that cities employ to attract business and investment. Residents that have lower housing costs are likely to stay in their neighborhoods and reinvest their income into the local economy, creating a multiplier effect that can benefit the entire community.

Property tax incentives with a direct approach should set the incentive to match the level of affordability the policy is aiming to achieve. Without an equitable match, a developer would not be incentivized to participate in the program. For example, consider a hypothetical policy designed to reduce rent by $100 per month for a targeted income group. An effective tax incentive to support housing for this group would have to be approximately equal to the reduction in rent. In this instance, if the tax incentive is valued at less than $100, then developers are not incentivized to produce the affordable unit, while incentives valued more than $100 would not be an efficient use of public revenue.



A direct $100 per month, or $1,200 annual, subsidy is required per unit.

Effective direct property tax incentives carefully evaluate the time period of the incentive to ensure that it aligns with the larger policy goals of the incentive. Programs may have an initial period that can be extended through a longer-term exemption. Many cities also designate the timing of the incentive based on the specific geographic area in which the development is taking place.

To target deeper levels of affordability through a property tax abatement, incentives should allow tax reductions for market-rate units to cross-subsidize units at deeper levels of affordability. In strong markets, market-rate units can shift tax incentives allocated toward a mixed-income building toward deeply affordable units, allowing for the unit to be affordable at lower incomes.

Cross-subsidizing Affordability in New York

As the quintessential “strong market,” New York City has always tried to reconcile high demand with limited land. The 421-a program allows full property exemption for 35 years if 25-30% of the units are reserved for low- to moderate-income tenants. The property exemption on the market rate units allows for deeper levels of affordability for the subsidized units, which have a larger gap between the rent required and what households can afford to pay. This program has been a significant part of Mayor de Blasio’s affordable housing plan and is important to achieving the City’s goal to build or preserve 200,000 below-market-rate apartments by 2022.

Recommendations

3. Effective property tax incentives enable simple administration and developer participation.

Tax incentives should rely on a rule-based approval process. These programs should be designed to work in tandem with an existing development process that is predictable and limits discretionary review. Clear and consistent affordability requirements can keep tax abatement programs from being an additional regulatory hurdle for developers. If tax exemptions require a negotiation, developers and city stakeholders should have clear guidelines over the terms of such a negotiation.

Administrative simplicity influences the effectiveness of tax incentives. Administering policies with greater complexity and difficulty requires more time and resources. An onerous process also discourages developers from participating in a program and developing units.

Policies should keep income documentation and reporting requirements simple and should not replicate burdensome federal requirements. Tax incentive requirements are locally controlled and are not required to follow the complex requirements of federally funded programs. Many local governments default to existing federal requirements for income documentation and monitoring requirements. Complying with overly complex income documentation and monitoring requirements can require additional staff and training, creating a significant cost for developers to participate in the policy.

Resident selection processes should not impede the process of filling rental housing. Resident screening requirements for eligibility to occupy an income-restricted unit should be clear and easy to incorporate into the standard screening process. Identifying income-eligible residents can be a significant added cost for property owners. To reduce costs, local governments should work with a nonprofit partner to identify a pool of eligible residents from which property owners can draw. Policies must also manage the legal regulations of the incentives. They need to ensure that developments that do not adhere to policy requirements lose incentive status and pay back the abated tax revenues to the city through a process known as a “clawback.” This type of feature can help assuage local opposition to tax incentives, which are sometimes perceived as a “giveaway” to developers.

Recommendations Summary

To design effective property tax incentives, a city should take a three-tiered approach.

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1) EFFECTIVE TAX INCENTIVES HAVE A DEFINED AND FEASIBLE APPROACH TO INCREASE AFFORDABILITY.

- Tax incentive policies should not only be limited to units that receive other federal and state subsidy sources.
- Tax incentives should be geographically targeted based on market conditions.
- The flexibility of tax incentives should be used to create an approach customized to a market. In markets where the supply of housing is limited by a lack of developable land, a direct approach is best.

2) EFFECTIVE PROPERTY TAX INCENTIVES BALANCE AFFORDABILITY REQUIREMENTS WITH INCENTIVES.

- Successful tax incentives can have economic, fiscal, and policy benefits that outweigh the implementation costs and foregone tax revenue.
- Property tax incentives with a direct approach should set the incentive to match the level of affordability the policy is aiming to achieve.
- Effective direct property tax incentives carefully evaluate the period of the incentive to ensure that it aligns with the larger policy goals of the incentive.
- To target deeper levels of affordability through a property tax abatement, incentives should allow tax reductions for market-rate units to cross-subsidize units at deeper levels of affordability.

3) EFFECTIVE PROPERTY TAX INCENTIVES ENABLE SIMPLE ADMINISTRATION AND DEVELOPER PARTICIPATION.

- Tax incentives should rely on a rule-based approval process. These programs should be designed to work in tandem with an existing development process that is predictable and limits discretionary review.
- Administrative simplicity influences the ability of tax incentives to be effective.
- Policies should keep income documentation and reporting requirements simple and should not replicate burdensome federal requirements.
- Resident selection processes should not impede the process of filling rental housing.

Economics of the Tool

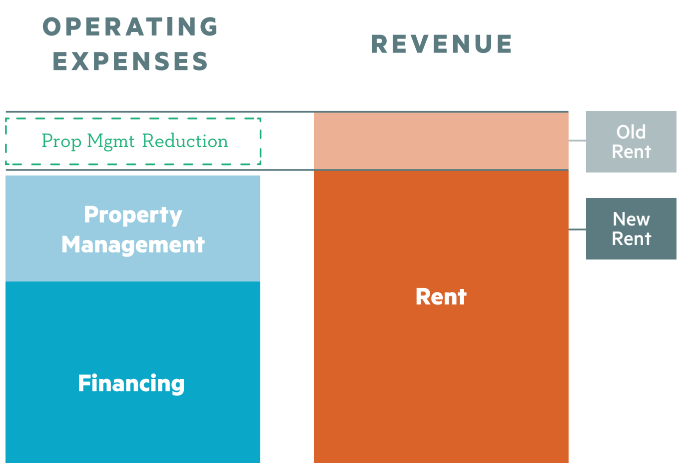
Tax incentive policies are designed to reduce operating expenses and the resulting rent required.

Direct Approach: Reduced Operating Expenses

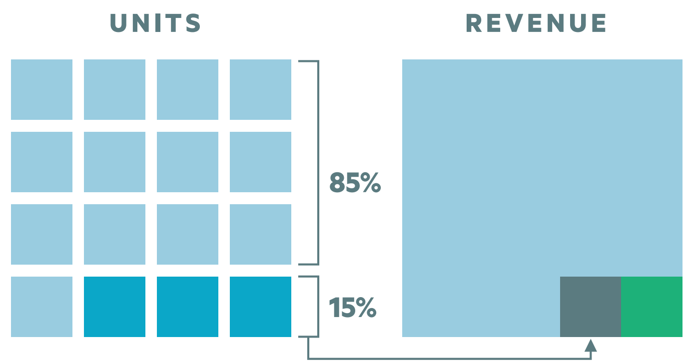
Tax incentives impact property management expenses directly by reducing the annual property tax paid by an owner. Lower property management expenses may also help underwrite more favorable financing terms.

A reduction in these costs leads to a lower amount of operating expenses required and a lower required rent to make the project viable. Policies that require affordability as a condition of tax incentive must ensure that the reduction in rent can be offset by the savings in operating expenses.

If the required rent for a project is $1,000 per month and a program is designed to create units that are affordable for households earning $30,000 or less, tax incentives must account for $250 per month per unit to make the project feasible. For this program to help 1,000 households, it would cost the city $3 million annually, plus additional administration costs, for each year that the units remain affordable.



For a mixed-income building, direct property tax incentives can be used to increase affordability for some of the units. For a hypothetical 100-unit building, if the required rent for a project is $1,000 per month and a program is designed to ensure that 15% of the units are affordable to households earning $20,000 or less (at $500 per month), a tax incentive could provide a tax incentive of $75 per unit. The market-rate units would be able to reallocate these savings toward the 15 units to account for their reduced rents.



With tax incentives, 15% of the units only need to account for 7.5% of the required rent

Market-Rate Units ($1,000/month)

Subsidized Units ($500/month)

Tax incentive subsidy

Economics of the Tool

Tax incentive policies are designed to reduce operating expenses and the resulting rent required.

Supply Approach

Tax incentives can increase affordability indirectly. As supply increases, it reduces competition for existing housing and leads to lower rents. This indirect impact can be significant. Below is the estimated[1] impact of a 1% increase in housing supply on rents and the number of households who would be able to afford rental housing as a result.

	DECREASE IN SHARE OF UNITS <$800 SINCE 2000 (PERCENTAGE POINTS)	EFFECT OF 1% INCREASE IN SUPPLY: REDUCTION IN RENT	EFFECT OF 1% INCREASE IN SUPPLY: INCREASE IN AFFORDABILITY (BY HOUSEHOLDS)
Atlanta	15.7	0.63%	690
Sacramento	19.5	0.98%	720
Minneapolis	15.1	0.95%	780
Denver	20.9	0.98%	1,300
Pittsburgh	21.1	1.19%	730
San Antonio	19.3	0.82%	720
Seattle	14.5	1.02%	1,500
Tampa	26.8	1.00%	580

1 A 2018 study by the Bay Area Council Economic Institute ("Solving the Housing Affordability Crisis") evaluated the effect of various housing policies based on the number of households for which housing would become affordable as a result of the policy, using a 30% housing cost burden assumption. The report evaluated the responsiveness of price to changing the supply through policy. Using a similar method, HR&A evaluated the number of households for which housing would become affordable, given a 1% increase in the overall supply of the eight case-study cities.

NATIONAL
MULTIFAMILY
HOUSING
COUNCIL

Tool: Rent Control

THE HOUSING AFFORDABILITY TOOLKIT

Developed in Partnership with
HR&A Advisors

Rent Control

Rent control is a counterproductive housing policy that does not address any of the key factors driving housing affordability.

What Is Rent Control?

Apartments have long provided people a flexible and inherently affordable housing option. However, as the number of renters has reached an all-time high, there has been a surge in demand. This has made it difficult for millions of families nationwide to find quality rental housing that is affordable across the income spectrum and has placed significant pressure on the available apartment supply. In response, some municipalities have tried to artificially restrict rents. While some of these rent control policies may be well intentioned, numerous studies have shown that rent control fails to increase the availability of affordable housing. Economists almost universally agree that rent controls reduce the quantity and quality of housing.[1]

Rent control regulations limit the amount of rent a landlord can charge, either by setting a rent ceiling or by limiting rent increase.[2] Currently, rent control regulations are in effect in four states and in Washington, D.C., while 36 states explicitly prohibit municipalities from implementing rent control.

How Rent Control Works

A set of price control regulations codify restriction on a city's rental housing market. The specific rules that govern rent control vary significantly between cities. Generally, these regulations establish which units rent control applies to, the conditions in which rent can rise, the amount of increase, how long rent control may remain in place, and processes for appeals and monitoring.

> **"The absurdity of New York City's housing market has become a standard part of many Econ 101 courses, because it is such a clear example of [rent control] that achieves the near opposite of its goals."**
>
> – Adam Davidson, *New York Times,* 2013.[3]

Rent control impacts affordability in three key ways

Rent control leads to a decrease in the supply of overall units and an increase in rents for unregulated units.

Rent control is an inefficient tool that often benefits high-income households as much as, if not more than, low-income households.

Rent control is complicated and expensive to administer.

1 NMHC, 2017
2 The Economist. "Do Rent Controls Work?," 2015
3 New York Times. "The Perverse Effects of Rent Regulation," 2013

Impacts

1. Rent control leads to a decrease in supply of overall units and an increase in rents for unregulated units.

Rent control leads to a decrease in the supply of overall units and an increase in rents for unregulated units. Studies across the country have found that forcing rents below market price has reduced the supply of new housing. This occurs in two ways:

1. Price ceilings make rental housing an unprofitable venture, and developers have less incentive to build. Money flows out of the local rental market and into more profitable markets.

Cambridge, MA ended rent control in 1995. As a result, annual investment expenditures more than doubled for all residential property from 1995 to 2004.

2. Property owners are incentivized to convert apartments into condos, which benefits higher-income households that can afford to own a home. The conversion of apartments to condos increases displacement **and creates a significant risk of displacement for existing residents.**

A study in Los Angeles, CA found that vacancy control resulted in a 7% decline in rental units as landlords converted apartments to condos.

These phenomena reduce the overall supply of housing and lead to increased competition for existing units – especially for those that remain unregulated. This drives up rents.

ACCELERATING GENTRIFICATION IN SAN FRANCISCO, CA

A Stanford Graduate School of Business study released in 2018 tracked the effects of rent control in San Francisco since their expansion of regulation in 1994. The study found that rent control reduced the supply of housing in the city by 6% and was responsible for more than 5% of the increase in rental prices of unregulated units. Additionally, rent control incentivized landlords to convert their properties into condos, further decreasing supply and raising rents. This may have accelerated gentrification in the Mission District, as smaller buildings that were once market-rate affordable housing rapidly became condos.

The study also found that the initial benefits of rent control helped existing tenants at the expense of new tenants. Tenants who lived in rent-regulated units before 1993 benefited by a net of $2.7B – exactly equal to the direct and indirect costs borne by new tenants living in unregulated units from 1993 onward. This created winners and losers and provided no overall benefit to tenants.

1 Author et al "Housing Market Spillovers: Evidence from the End of Rent Control in Cambridge, MA." Journal of Political Economy, University of Chicago, 2014
2 Ellis Act Evictions, Anti Eviction Mapping Project, 2018
3 Stanford Graduate School of Business. "Rent Control Winners and Losers," 2018

Impacts

2. Rent control is a blunt tool that does not efficiently target benefits.

Rent control is a blunt and inefficient tool that often benefits high-income households as much as, if not more than, low-income households. Rent control regulations are tied to units instead of households, and a rent-controlled unit can go to a household of any income. Low-income households must compete with higher-income households for rent control and receive no preference. There is significant evidence that this leads to a large and often arbitrary subsidy that can benefit households able to afford market-rate rents.

A 2000 study by the San Francisco comptroller found that 25% of rent-controlled units were occupied by households with incomes over $100,000.[1]

In 2012, the NYU Furman Center found that the median income of households in prized rent-stabilized units in Manhattan was higher than the median income of market-rate residents in all but eight neighborhoods across all five boroughs.[2] Higher-income residents in Manhattan paid less for their apartment than lower-income households in the cheaper markets of Brooklyn and Queens.

A study in Cambridge, MA found that households in rent-controlled housing had higher incomes than the citywide average, including the average incomes of homeowners.[3]

There are a number of reasons that rent-controlled apartments are more likely to end up with higher-income households residing in them. When a household leaves a rent-controlled apartment, the residents often "pass on" the apartment to someone in their social network in the same income level. In Los Angeles, there is evidence of a gray market of "key fees" that require potential tenants to pay a significant up-front cost for a rent-regulated unit. This practice further restricts lower-income households from accessing affordable, regulated units.[4]

Households in rent-controlled housing in Cambridge, MA had higher incomes than the citywide average.

1 New York Times, "San Francisco Rent Control Unintended Consequences," 2012
2 NYU Furman Center, 2012
3 Goetze, "Rent Control: Affordable Housing for the Privileged, Not the Poor," 1994
4 L.A. Weekly, "L.A. Moves to Curb "Cash-for-keys" Rent-Control Landlord Scams," 2016

Impacts

3. Rent control is complicated and expensive to administer.

Rent control requires elaborate bureaucratic systems. Rental property must be registered, detailed information on the rental property must be collected, and elaborate systems for determining rents and hearing complaints and appeals must be established. The associated costs in dollars and time falls not only on providers, but also on consumers and municipal authorities.

For example, in Santa Monica, the Rent Control Board in 1996 had a budget of more than $4 million a year to control the rents for only 28,000 apartments.

Denver's housing stock consists of 72,200 multifamily rental units that were built before 2000, which represents about half of the city's entire rental housing stock. These units vary widely in scale, owner type, and current leasing arrangements. To enact a rent control policy, the contracts of each of these units would need to change and be regulated by the city.

> **This would cost Denver an additional estimated**
> **$10 MILLION**[1]

1 Based on the cost of rent control administration in Santa Monica, CA, at $142 per unit annual

Considerations

Rent control does not address any of the key factors driving housing affordability challenges.

An insufficient supply of rental housing, rising development and operation costs, and stagnant incomes are the factors driving growing housing affordability challenges. Cities must address these key factors to address affordability. Rent control does not address any of these factors.

- Rent control decreases supply. Studies have shown that rent control leads to an overall decrease in supply as landlords convert units to condos and developers cannot bring units to market.
- Rent control increases administrative operation costs. Rent control adds compliance costs and the overall cost to operate rental housing.
- Rent control is not tied to those who need it. It does not provide a targeted subsidy for lower-income households who need assistance the most.

Rent control seeks to treat the symptom of rising rents without addressing these underlying factors. This leads to unintended consequences that shifts the affordability burden among tenants and often decreases overall housing affordability. Improving housing affordability means closing the gap between what a household can afford and what it costs to develop and operate rental housing. It also includes ensuring that the supply of rental housing can keep up with rising demand.

Local governments have many tools at their disposal that can decrease the affordability gap and increase overall supply. Rent vouchers can help increase what households can pay for units. Tools like property tax incentives, public land subsidies, and other developer incentives can decrease the cost to develop and operate housing, while expanding by-right development can help increase overall supply.

Economists have long considered rent control a failed housing policy – the benefits for a few select tenants do not outweigh the substantial economic and social costs. Cities around the country have shown that these policies have led to higher rents and fewer units overall.[1]

1 New York Times. “Why Rent Control Is a Lightning Rod,” 2018