

Director's Report
Relating to Affordable Housing Incentives
May 19, 2017

I. PROPOSAL SUMMARY

The purpose of this bill is to provide incentives to help stimulate affordable housing production, especially rental housing, and to offset impacts of the proposed Affordable Housing Requirement (AHR; see companion AHR bill). Mayor Caldwell and the Affordable Housing Workgroup recommended these incentives as part of the overall Affordable Housing Strategy. The proposed incentives will provide exemptions to real property taxes and waivers for wastewater system facility charges, plan review and building permit fees, and park dedication requirements for projects providing affordable dwelling units, as described in the bill summary below.

Title	Affordable Housing Incentives Bill
Summary	Amends the Revised Ordinances of Honolulu (ROH) to provide incentives to support the creation of affordable housing provided through: <ol style="list-style-type: none">1) The City's proposed Affordable Housing Requirement (AHR);2) The Planned Development-Transit (PD-T) permit (Bill 74 (2015)) and the Interim Planned Development-Transit (IPD-T) permit (ROH 21-9.100) (prior to the adoption of the AHR bill); and3) Qualifying affordable rental housing projects (per Hawaii Revised Statutes 201H-36(a)(5)).
Scope	<p><u>Adds new</u> ROH sections (number to be designated after adoption):</p> <ul style="list-style-type: none">• Section 8-10.___, dealing with annual real property tax exemptions for affordable rental dwelling units• Section 8-10.___, dealing with real property tax exemptions during the project's construction period for a maximum of three years• Section 14-10.___, dealing with waivers for wastewater system facility charges (connection fees) for affordable dwelling units <p><u>Amends existing</u> ROH sections:</p> <ul style="list-style-type: none">• Section 18-6.5, dealing with waivers for plan review and building permit fees for affordable dwelling units• Section 22-7.4, dealing with waivers for park dedication requirements for affordable dwelling units
Effective Date	Upon adoption
Expiration Date	Ten years after the ordinance's adoption, except for the real property exemption provisions for affordable rental units which will continue for the entire required period of affordability.

II. BACKGROUND

As described in the Mayor's Affordable Housing Strategy (September 2015), the need for affordable housing on Oahu is high and continues to increase. This bill provides incentives to support the creation of affordable housing units provided through 1) The City's proposed AHR; 2) PD-T and IPD-T permits; and 3) qualifying rental housing projects pre recent state legislation.

- 1. Affordable Housing Requirement.** One of the key actions identified in the Affordable Housing Strategy is to increase affordable and workforce housing inventory by adopting an AHR. While current regulations applied to rezoning require affordability to be maintained for 10 years or less, the AHR will prioritize more affordable rental housing for lower income households, require affordability for three times longer, and have sufficient flexibility to meet developers' needs. The AHR bill is being introduced to Council for adoption along with this incentives bill. The AHR bill establishes an islandwide affordable housing requirement (e.g., for housing below market rates) for most new private development and substantial rehabilitation of dwelling units. The AHR will apply to projects of 10 or more dwelling units. Affordability is targeted towards household renters earning at or below 80 percent of the AMI and homeowners earning at or below 100 percent and 120 percent of the AMI. The AHR varies by location and will be phased in over three years to account for the different housing market conditions on Oahu. Due to different development types and circumstances, the AHR includes flexibility so that it can be met through a variety of ways: for sale or rental dwelling units, production on-site or off-site, a \$45 per square foot in-lieu fee in rail station areas (\$27 per square foot islandwide), and/or conveyance of improved land. The proposed in-lieu fee is set at an amount to encourage actually building units. The affordable units are required to stay affordable for at least 30 years to build up and maintain the quantity of affordable units over time. The objective of the AHR is to develop and maintain a stable, growing affordable housing stock for residents. More information about the AHR is provided in the Director's Report of the companion AHR bill.
- 2. Planned Development–Transit and Interim Planned Development–Transit Permits.** The areas near the future rail transit stations will undergo zone changes and be included in a new transit-oriented development (TOD) special district that includes TOD-specific development regulations. In the meantime, landowners may apply for an IPD-T permit to seek additional height and/or density, and development flexibility in use and other regulations in exchange for community benefits, such as affordable housing, open space, and circulation improvements. This bill provides incentives to support affordable dwelling units provided through IPD-T permits. Once a station area is adopted into the TOD special district, landowners may still apply for a PD-T permit to seek similar flexibility on eligible lots. This ordinance would provide the same incentives for any affordable housing units provided through PD-T permits. Once the AHR bill is adopted, it will regulate the minimum affordable housing required under the IPD-T or PD-T permits, except for additional housing provided in return for bonus density and/or height (more than double the existing density).
- 3. Qualifying Rental Housing Projects.** There is a strong demand for affordable rental units, which is exacerbated by the difficulty the private sector has in producing unsubsidized rental housing because of the challenging economics of building and operating rental housing in Hawaii. In an effort to address the high demand for rental units, the State legislature recently passed House Bill 1179 (bill not yet signed), which amends HRS Section 104-2 to establish a special prevailing wage rate for construction of qualifying projects, and HRS Section 201H-36 to provide exemptions from the general excise tax for qualifying rental housing projects. For projects under HRS 201H-36(a)(5), all rental housing units must be offered to households at

or below 140 percent of the AMI, and 20 percent of the units must be offered to households earning at or below 80 percent of the AMI. While 140 percent of the AMI range is higher than the City's AHR affordability range, the incentives should conform to the State legislation under this program. State agencies regulate the period of affordability and penalties for those projects that fail to comply with their requirements. The City's incentives bill is intended to complement the State's incentives, by providing additional incentives for qualifying rental housing projects in an effort to support the production of affordable rental housing.

III. ANALYSIS

Many local jurisdictions have adopted AHRs. In many cases, cities and counties offer fee waivers, streamlined review processes, additional height or density, or other incentives to encourage affordable housing. Providing financial incentives results in an AHR that is workable for both the community and developers. Some analysis have shown that providing significant incentives can, in some markets, substantially reduce or even eliminate any loss of profit to the developer. While that is less likely in expensive housing markets like Oahu, reduction or elimination of fees and regulatory conditions can significantly decrease the financing gap between market rate units and affordable units, which will help get the affordable housing supply built. The General Plan recommends incentives in Objective A, Policy 7: Provide financial and other incentives to encourage the private sector to build homes for low- and moderate-income residents.

Affordable Housing Incentives Proposal. This proposal will provide temporary financial incentives by waiving certain City fees for affordable housing units. The intent is to stimulate affordable housing production by offsetting the AHR that is being introduced by the City. Several agencies worked together to provide these incentives, including the Department of Planning and Permitting (DPP), the Mayor's Office of Housing, the Department of Environmental Services (ENV), the Department of Parks and Recreation, and the Department of Budget and Fiscal Services (BFS). The City received significant input about the need for financial incentives from housing organizations that were participated in the Affordable Housing Working Group. The group included developers, finance experts, industry representatives, affordable housing advocates, and key City staff. Both developers and housing advocates were in favor of providing these affordable housing incentives.

Current fee requirements and proposed waivers include:

- The DPP currently charges a plan review and building permit fee to all new development based on a project's construction cost (building permit fee schedule is established in Chapter 18, Table No. 18-A). Plan review fees are 20 percent of a tentative building permit fee. The proposed incentive is to waive the plan review and building permit fees for the affordable dwelling units.
- The ENV currently requires newly built residential units receiving wastewater facility service to pay a one-time, per-unit charge. The wastewater system facility charge is established in Chapter 14, Appendix 14-D. The current wastewater system facility charge per equivalent single family dwelling unit is \$6,616 for fiscal year 2016/2017 (for qualifying low-income housing units the fee is \$1,368 per equivalent single family dwelling unit). Under the proposed incentive, the wastewater system facility charge would be waived for the affordable dwelling units.
- The DPP currently requires developers of most new residential projects to dedicate a portion of land for use as a park or playground, or to pay a fee equivalent to the fair market value of the land that would be dedicated. Under the proposed incentive, the park dedication requirement would be waived for the affordable portion of the project.

- The BFS currently levies real property tax on most properties. Under the proposed incentive:
 - There would be a tax holiday (during construction) for those projects with affordable dwelling units. Real property taxes would be kept at the current assessment during the project's construction period for up to three years or until construction is completed.
 - An ongoing annual exemption would be provided exclusively for rental dwelling units. The real property tax exemption for rental units will continue during the required period of affordability, as established in an affordable housing agreement.

The proposal stipulates that the financial incentives will be repealed after 10 years, although the real property tax exemption provisions for rental units will continue for the entire required affordability period as stipulated in an affordable housing agreement.

Affordable Housing Requirement Financial Analysis. The City's consultant, Strategic Economics, evaluated the ability of residential real estate development to support the proposed AHR. The analysis concluded that the AHR represents a modest cost burden on development compared to total development costs—the net costs of the required affordable units would comprise 1 to 5 percent of a condominium project's total development costs and 3 to 6 percent for a rental apartment project. The financial incentives through fee waivers could reduce costs by 1 to 3 percent, helping to offset the costs associated with providing the affordable units.

Affordable Housing Incentives Fiscal Impact Analysis. Strategic Economics also conducted a fiscal impact analysis of the proposed incentives for units constructed under the AHR over a 10-year period. The analysis examined the impacts of waiving wastewater facility charges, plan review and building permit fees, and park dedication requirements for all affordable units, and exempting the real property tax for affordable rental units. The fiscal impact of the real property tax exemption during construction was not included in the analysis, because during the construction period, real property tax will be based on the preceding tax year's assessment. Such analysis would require estimating the current property tax assessments of potential future projects, which is not feasible. The exemption will defer property tax increases until construction is completed.

The analysis assumed that over 10 years, 1,500 units would be provided through the AHR, of which 10 percent are single family, 15 percent multi-family rental, and 75 percent multi-family for-sale condos. Assumptions for the annual growth in wastewater facility charges, home values, construction costs, assessed value of affordable rental units, and land value were also included in the analysis. The financial impact for the park dedication requirements waiver is presented separately. Calculating a dollar figure for the park dedication requirement waiver requires estimating the value of land. However, it is difficult to know what land values will be for new development, because it depends on where development would take place over the next 10 years. Land value assumptions in the Affordable Housing Requirement Financial Analysis ranged from \$45 per square foot in Kapolei for a single family unit to \$375 per square foot in Ala Moana for a multi-family unit. For these reasons, the park dedication dollar figure is presented in a range that considers lower and higher land values.

Since the qualifying affordable rental housing project under HRS 201H-36(a)(5) is a new project type not currently being produced, no projections were created for the number of units that these projects could provide per year, over the next 10 years. The fiscal impact analysis was based on a model with 100 units. The fiscal impact analysis provides a scenario of the projected costs of the proposed incentives. These costs are balanced by the multiple direct and indirect benefits to the community that result from increasing the supply of affordable housing.

AHR, IPD-T, and PD-T

One-Time Fee Fiscal Impacts to City Revenues

The 10-year average for the one-time fees waived per year would be:

- Plan review and building permit fee waivers \$220,000
- Wastewater system facility charges waiver \$820,000
- Park dedication requirement waiver from \$3,650,000 to \$8,500,000*

Per unit the average one-time fees waived per year would be:

- Plan review and building permit fees and wastewater system facility charges \$7,800
- Park dedication requirement only from \$24,000 to \$57,000
- Total one-time fees waived from \$32,000 to \$64,000

* Assuming land values of \$150 and \$350 per square foot for multi-family, and \$25 and \$50 per square foot for single family.

Real Property Tax Exemptions for Affordable Rental Units**

The 10-year average for real property tax exemptions per year would be: \$130,000

For the first 3 years the exemptions for real property taxes for rental units are below \$100,000; by year 10 the foregone revenues increase to \$270,000 per year.

**Ongoing Annual Impacts: Rental property tax exemptions will be ongoing, with both repeating waivers per unit and new units produced each year. This yields an increasing and cumulative effect each year.

Qualifying Rental Housing Projects (HRS 201H-36(a)(5))

One-Time Fee Fiscal Impacts

The one-time exemption for a 100-unit qualifying affordable rental housing project would be:

- Wastewater system facility charges \$390,000
- Plan review and building permit fees \$150,000
- Park dedication requirement \$1,750,000 to \$2,900,000**

Per unit, the total one-time fees waived would be: from \$23,000 to \$35,000

**Assuming land values of \$150 and \$250 per square foot and that rental projects will not be located in areas with higher land values.

Real Property Tax Exemptions for Affordable Rental Units***

For the qualifying affordable rental housing projects under HRS 201H-36(a)(5), assuming the 100-unit model described above, the average real property tax exemption per year would be \$230,000 or \$2,300 per unit (assuming an affordability period of 30 years).

Per unit, the real property tax exemptions over 30 years would total \$69,000.

***Ongoing Annual Impacts: Rental property tax exemptions will be ongoing, with both repeating waivers per unit and new units produced each year. This yields an increasing and cumulative effect each year.

IV. CONCLUSION

Based on the stakeholder discussions, extended research by City staff, and the financial and fiscal impact analysis, the DPP Director recommends adopting the incentives outlined above. The Directors of the affected departments support these recommendations. The proposed incentives will help spur affordable housing production to meet identified needs.

At the Mayor's request, the Board of Water Supply (BWS) is exploring how to provide similar incentives for affordable housing. As a semi-autonomous city agency, the Board of Directors for the BWS determines any rate changes. Therefore, no waiver for water hook-up charges has been included in this bill.

The ultimate purpose of providing these affordable housing incentives is to enhance public welfare, by adopting policies that increase the housing inventory in the city in a manner consistent with State and local housing policies and needs, and by making housing available to households at all income levels.