MEMORANDUM

TO: Mayor Appelbaum and Members of City Council

FROM: Karen Rahn, Director, Housing and Human Services
Jeff Yegian, Acting Housing Division Manager
Michelle Allen, Housing Planner

DATE: March 29, 2012

SUBJECT: Study Session April 10, 2012
Inclusionary Housing Rental Policy Update

I. PURPOSE

The purpose of this item is to update City Council on proposed 2012 Inclusionary Housing (IH) rental project issues. Depending on council direction, an update to the IH rental policies would likely include the need for code changes. Since IH is included within the Land Use chapter of the Boulder Revised Code, staff would be taking any proposed code changes to the Planning Board for a review prior to coming to council for adoption.

This IH rental policy update has been anticipated since the long term housing development market changes became apparent. The volume of proposed rental development makes this project time-sensitive.

II. QUESTIONS FOR COUNCIL

To assist staff in preparing rental policy options for council review and consideration, feedback is requested on the following questions:

1. Does council have questions concerning IH as it applies to rental projects?
2. Should the city pursue affordable housing tools, other than IH, that provide incentives for mixed income rental projects with affordable homes integrated with market-rate units?

III. BACKGROUND

Like many communities in Colorado and nationwide, Boulder struggles to create and preserve affordable housing in an environment where home price increases have significantly outpaced income growth. For workers earning $10 per hour, an affordable rent (25 percent of income absent utilities) is approximately $430 per month. In the fourth quarter of 2011, the average monthly rent in the Boulder and Broomfield counties was $1,038 according to the Colorado Division of Housing. High housing costs and limited housing options diminish Boulder's economic diversity and contribute to the decision of some moderate and lower wage employees, such as teachers, health care workers, service and retail workers and childcare providers, to either pay more than 30 percent of their income for housing, compromising their ability to pay for other basic needs, or meet their housing needs elsewhere and commute to employment in Boulder.

The IH ordinance, which requires 20 percent of all new residential development be permanently affordable, was adopted in 2000 to mitigate the impacts of rising housing costs. Through 2008, almost all residential development in Boulder was ownership housing. During this time, the IH program resulted in 364 permanently affordable ownership units and $9,053,697 in cash-in-lieu (CIL) contributions, which was used primarily to obtain, develop and maintain affordable rental housing. As anticipated in the IH ordinance, about half of the required affordable units were provided on-site within new developments.

As a result of the 2007 and 2008 financial crisis, the capacity and willingness of the private financial system to support real estate lending declined. Developers have been less able to obtain financing to construct ownership housing, and potential homebuyers were both less able to sell their homes and finance new purchases. Since then, almost all new and proposed residential development projects in Boulder have been rental housing.

Legal Constraint on Rent Control

Colorado's statute banning rent control, CRS 38-12-301 (*Attachment A - Summary of State Statute CRS 38-12-301*), substantially complicates the application of IH to rental housing. This statute instituted a statewide rent control ban to ensure that, notwithstanding home rule authority, no city or county in Colorado would, as a matter of law, be able to institute a rent control measure. Shortly after the city adopted the Inclusionary Zoning Ordinance in 2000, the Colorado Supreme Court held that the imposition of rent control as a choice among other rent or ownership options in an Inclusionary Zoning ordinance violated the state rent control prohibition. Thereafter, the city amended its Inclusionary Zoning Ordinance to limit rent control provisions to an exception in the statute that allowed housing authorities and similar agencies to impose rent control.

To meet the requirements of the state statute under the city's current policy, rent-controlled units provided on- or off-site must be owned in whole or in part by a housing authority or similar agency. Rental developments are typically not subdivided or otherwise split in to separate legal entities like condominiums. Having mixed or joint ownership would complicate project financing, property management, property taxes, insurance and land use requirements. In addition, Boulder has a limited number of active "similar agencies" that have the funding and capacity to acquire rental units that result from IH. Due in part to the Colorado rent control prohibition, no affordable rental units have been integrated within new rental developments.

Around 2009, when the shift in the housing market from development of ownership units to rental units became more apparent, staff anticipated a corresponding shift in the outcomes from the IH program. At that time, the Affordable Housing Task Force process was beginning and it was important to understand its members' perspectives and get their input. In addition, it was important to observe how IH responded to rental development and to gauge the intensity and duration of the shift before recommending any substantive changes to the program. *(Attachment B - Inclusionary Housing Outcomes)*

IH Outcomes

When applying the IH requirements to rental developments, staff has observed trends inconsistent with the desired outcomes of IH and the Boulder Valley Comprehensive Plan (BVCP) policy on dispersion of affordable units. In addition, some IH policies are not well suited to rental characteristics and constraints. The primary identified outcomes of the city's affordable housing program may be found in the IH ordinance. Applying them equally to both ownership and rental developments may be resulting in unintended or undesirable outcomes. Two principal IH outcomes and the BVCP policy are listed below, followed by observations about rental development.

<u>IH Desired Outcome</u>: Affordable units should be integrated into each residential development resulting in mixed income developments. To this end, half of the required affordable units in ownership developments should be provided on-site.

<u>Rental Development Outcome:</u> Affordable rental units have not been provided on-site, nor have they been integrated into new residential development. Financial and land use realities combined with the restrictions imposed by the state statute prohibiting rent control have made this outcome difficult to achieve. Consequently, on-site rental units are encouraged but not required in the IH Ordinance. The state statute means it is unlikely that IH will result in on-site rental units. However, there may be other tools including voluntary agreements with subsidies and/or incentives such as density bonuses and fee waivers that could be offered to rental developers in return for on-site affordable rental units. Further research and analysis is needed to fully understand the costs and benefits of such approaches.

<u>IH Desired Outcome</u>: Each new residential development should provide 20 percent of the units as permanently affordable or otherwise contribute to the city's affordable housing goals.

<u>Rental Development Outcome</u>: It is not a given that a requirement of 20 percent of ownership units is equivalent to 20 percent of rental units. There are many differences between the two types of development, including the cost to produce units, expected returns to investors, targeted household incomes, availability and types of financing and operating characteristics. In addition, CIL amounts for both types of development are currently based on the ownership affordability gap[1]. While it is impossible to ensure that IH has the same impact on each development, one component of IH is that each residential development contributes equally.

Planned IH Rental Update Activities: Staff anticipates completing an analysis of the differences in IH costs and impacts to homeownership and rental development, which will include:

- rental developer interviews
- rental and ownership pro forma analysis
- financial considerations
- target incomes and resulting rents
- basing CIL for rental projects on the rental affordability gap.

This analysis will inform new or modified IH requirements and policies for rental development that would result in equitable economic incentives for both types of development. Options for council consideration for IH policies for rental developments

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[1] The ownership affordability gap is the difference between the price of a market unit and comparable affordable unit.

may include adjustments to the percentage requirement, CIL amounts, and incomes served.

<u>BVCP Policy</u>

Policy 7.14 states that affordable units should be dispersed throughout the community.

<u>*Rental Development*</u>*: Since the on-site option has not been used for rental development, developers primarily utilize the CIL and off-site options. In the last two years, three projects have provided the required affordable units off-site, while only one project chose the off-site option in the preceding nine years. Based on discussions with developers currently in development review, use of the off-site option is anticipated to continue. One development has provided 56 affordable units off-site in two all-affordable projects near each other in North Boulder*[2]*. These projects raise questions about the number of affordable units in an off-site development and a possible future concentration of units in locations where vacant land is available and affordable.* (Attachment C – Distribution of Affordable Housing) *Currently, there is no specific language in the IH ordinance concerning where or how off-site units may be provided. A provision in the IH Administrative Regulations states that off-site locations and units are approved at the sole discretion of the city.*

Planned IH Rental Update Activity: Further criteria are needed to guide approval of off-site locations and will be developed as part of the IH program policies.

Inclusionary Housing Policies

In the early years of the IH program, with very few rental projects to use as test cases, it was unclear, particularly after the Colorado Supreme Court decision, how the IH program would function for rental projects. Over the past two years the city has applied IH to several rental developments and found that the consequences of the state statute and the differing legal, ownership and financing characteristics of residential rental development require a new set of IH policies and procedures specific to rental projects.

Planned IH Rental Update Activity: Staff will examine current IH policies that are problematic for rental development including: household incomes served, the amount of CIL, required unit floor area, ownership and security requirements for off-site units, and criteria for the density and location of off-site units. *(Attachment D - Inclusionary Housing Policies to be Reviewed)*

Staff has been utilizing a provision of the IH Ordinance that allows for an alternative method of compliance to address policies that are designed for ownership, but are problematic for rental development. This has been used as a temporary approach until consistent, permanent policies can be instituted.

Planning Board Feedback

The Planning Board was updated on the contents of this memo on Feb. 2, 2012. Planning Board asked if it is necessary to offer the off-site option. The Deputy City Attorney responded that since IH is based on a land use requirement, a unit option was necessary. A contribution of CIL of units provides an option to the 20 percent IH unit requirement. Having CIL as the only option would result in something that is more like a fee and would have TABOR implications.

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[2] Staff is preparing an Information Packet item for April with information about the distribution of affordable housing in Boulder.

Planning Board also asked about the outcome of the Violet Crossing development. Staff replied that while the developer wanted to provide the affordable units on-site, that outcome proved challenging and the developer has agreed to pay CIL of units (*since this PB meeting the developer has indicated he will continue to pursue an off site option*). Staff observed that this project is a good example of why the IH rental policy update is needed.

IV. NEXT STEPS

The IH rental policy update process would take approximately one year before ordinance changes are adopted. Once complete, changes will go into effect. An additional several months will be required for drafting of the administrative regulations, review by Planning Board and adoption by the city manager.

1. First Quarter 2012: Consultant interviews with stakeholders, analysis
2. Second Quarter 2012: Development of program options
3. Third Quarter 2012: Planning Board and council meetings on program options and policies; develop ordinance language
4. Fourth Quarter 2012: Planning Board and council meetings to adopt ordinance language
5. Second Quarter 2013: Planning Board review and city manager adoption of updates to the IH Administrative Regulations

ATTACHMENTS

A – Summary of State Statute CRS 38-12-301
B – Inclusionary Housing Outcomes 2000-2011
C – Distribution of Affordable Housing
D – Inclusionary Housing Policies to be Reviewed

Summary of State Statute CRS 38-12-301

The state has a statute that prohibits the enactment of rent control in rental housing. Shortly after the city adopted the Inclusionary Zoning ordinance, now the Inclusionary Housing (IH) ordinance, the Colorado Supreme court held that the imposition of rent control as a choice among many other rent or ownership options in an Inclusionary Zoning ordinance violated the state rent control prohibition. Thereafter, the city amended its Inclusionary Zoning ordinance to limit rent control provisions to an exception in the statute to housing authorities and similar agencies.

Colorado's statute banning rent control, CRS 38-12-301, came as a result of a 1980 citizen initiative in the City of Boulder, which imposed rent control on existing buildings. At that time, the state legislature instituted a statewide rent control ban to ensure that, notwithstanding home rule authority, no city or county in Colorado would, as a matter of law, be able to institute a rent control measure.

Subsequently, the Town of Telluride enacted an Inclusionary Zoning ordinance for non residential property developments that allowed property owners to either build new units with fixed rents, by paying fees in lieu of building new units, or by conveying land to the town for affordable housing. In the case that went to the Colorado Supreme Court, a non-residential development was required to create permanently affordable rental housing for 40 percent of the employees generated by the new development.

In 2000 the court found that Telluride's Inclusionary Zoning ordinance was a form of rent control prohibited by CRS 38-12-301, and held that the ordinance was invalid and unenforceable. Despite being a "home rule municipality" with broad powers over local matters, according to the court, Telluride lacked the authority to impose rent controls because the legislature determined that rent control was not merely a local issue, but one that might affect other jurisdictions as well:

> *"Ordinances like Telluride's can change the dynamics of supply and demand in...the housing market. A consistent prohibition on rent control encourages investment in the rental market and the maintenance of high quality units. Although economic conditions may vary in housing markets across the state, the legislature has seen fit to enact a uniform ban on rent control as a matter of public policy."*

Section 38-12-301, C.R.S., titled "Local Control of Rents Prohibited" states the following:

> *"The general assembly finds and declares that the imposition of rent control on private residential housing units is a matter of statewide concern; therefore, no county or municipality may enact any ordinance or resolution which would control rents on private residential property. This section is not intended to impair the right of any state agency, county, or municipality to manage and control any property in which it has an interest through a housing authority or similar agency."*

As a result, the City of Boulder, as a result of advice from the City Attorney's office, can only accept permanently affordable rental units if they are owned by the housing authority or a non-profit with which we have executed a "similar agency" agreement that states that the non-profit is an agency that functions similar to that of the housing authority.

Inclusionary Housing Outcomes 2000-2011

The following table includes all developments with five for more dwelling units. All developments with two to five dwelling units met their IH requirement through cash-in-lieu (CIL). Single homes typically meet the requirement through a CIL contribution which, for owner/builders may be deferred until subsequent sale of the property.

	Total #	100% On-site	On-site & CIL	On-site & CIL & Off-site	100% Off-site	100% CIL
2000-2009	**51**	**28** (55%)	**10** (20%)	**1** (2%)	**0**	**12** (24%)
2010-2011	**14**	**1** (7%)	**0**	**0**	**3** (21%)	**10** (71%)

ATTACHMENT C

Distribution of Affordable Housing in Boulder

As of Jan. 1, 2012, 6.9 percent of Boulder's housing stock consisted of affordable units (2,995 of 43,617 units) dedicated for very low, low and moderate income households and 100 middle income affordable units dedicated for households earning on average 100 percent of the median income. This count includes units with permanently affordable deed restricting covenants, units likely to remain affordable and 242 shelter and group home beds.

Boulder's mix and location of affordable housing stock reflects, to a large degree, land development patterns in Boulder. Most of the permanently affordable housing units in Boulder were created after 1990. About half of the units gained within the last eleven years through the IH program have been provided on the site of new development and therefore reflect the location and type of housing created by the market. City-funded units reflect the needs and opportunities identified by affordable housing providers, with new units developed where land is available and residential development is permitted by current zoning and land use regulations.

The proportion of affordable units in Boulder sub-communities varies, with two sub-communities having over ten percent of their housing stock affordable.

	Affordable Units	**2012 Dwelling Units**	**% Percent of Affordable**
Central Boulder	718	13,256	5.42%
Colorado University	44	2,003	2.20%
Crossroads	665	3,782	17.58%
East Boulder	91	1,193	7.63%
Gunbarrel	2	725	0.28%
North Boulder	803	5,632	14.26%
Sub-areas:			
North of Violet	*686*	*1,954*	35.11%
Yarmouth North	*288*	*558*	51.61%
Palo Park	84	927	9.06%
South Boulder	127	7,263	1.75%
Southeast Boulder	461	8,836	5.22%
TOTAL	**2,995**	**43,617**	**6.87%**

[Data as of 1/1/2012 for Area I only (within city limits)]

- The highest proportion of affordable housing is found in the **Crossroads** sub-community, with **17.6 percent** of units affordable.
- The second highest percentage is **North Boulder**, with **14.3 percent** of units affordable.

- The **Palo Park** sub-community has **9.1 percent** affordable. However, if the approximately 680 market-rate units in Palo Park located just outside the city limits are included the proportion of affordable housing is **5 percent**.
- Three sub-communities, **East Boulder, Central Boulder**, and **Southeast Boulder**, consist of **between 5.2 and 7.6 percent** affordable housing.
- Three sub-communities, **Colorado University**, **South Boulder**, and **Gunbarrel** consist of **less than 2.2 percent** affordable housing.

Affordable Housing in North Boulder

The 1995 North Boulder Subcommunity Plan envisioned the creation of medium-density and mixed-use development north of Yarmouth Avenue and in the Village Center between Violet Avenue and Yarmouth Avenue. The land use designation in this area consists primarily of mixed-use residential, mixed-density residential, and mixed-use business (in the village center) in order to implement the sub-community plan. The city worked with Boulder Housing Partners (BHP) to purchase the Holiday Drive-In parcel in 1997 to provide a mixed-use and residentially-focused development. Approximately 40 percent of the homes in the neighborhood are permanently affordable, meeting a goal for the city's investment and BHP's participation. Council approved zoning that included a density bonus and waived most of the site development fees to encourage the creation of affordable workforce housing.

Housing in the North Boulder subcommunity (roughly north of Iris Avenue) consists of 14.3 percent affordable housing, the second-highest among Boulder's nine sub-communities. The area north of Violet Avenue consists of 35.1 percent affordable housing. The "Yarmouth North" area includes the Holiday Neighborhood and adjacent development north of Yarmouth and east of Broadway and consists of 51.6 percent affordable housing.

Future Trends

Most easy-to-develop land within Areas I and II has been developed. Constraints on future development include not only land use policies, but the difficulty of assembling and clearing sites that have multiple ownerships, existing buildings and/or environmental issues. In addition to North Boulder, significant development potential under the current Land Use map exists primarily in the Crossroads and East Boulder subcommunities, associated with Boulder Junction (the Transit Village Area), and in Gunbarrel, associated with the Gunbarrel Town Center Plan. Given the options for complying with IH (on-site, off-site, CIL, land dedication) and the unpredictability of project development, it is difficult to project how future development will affect the current distribution of affordable housing.

ATTACHMENT D

Inclusionary Housing Policies to be Reviewed

The following is a list of Inclusionary Housing (IH) policies that will be reviewed as part of the IH Rental Policy Update process. As work on the policies progresses and IH is applied to additional rental developments, other policies may be added for review.

1. Households served - Compliance with IH should result in rental housing affordable to households earning around 60 percent of the Area Median Income (AMI).[3]

Issue - Rents set to be affordable to the target household income are comparable to some of what can be found in the private rental market. As a result, the rental housing created through IH may not meet the needs of lower income residents. It also may be difficult to rent as some households would not want to income qualify when similarly priced rentals are available without completing that process.

2. Amount of cash in lieu (CIL) of providing affordable units - The CIL amounts are currently based on ownership affordability gap[4], not a rental affordability gap.

Issue - As rental developers appear very motivated to provide the required affordable units off-site, it may be that the CIL exceeds the amount needed to subsidize development of rental units. A disparate economic impact on different types of projects influences project selection and may distort development incentives.

3. Affordable unit sizes may be 80 percent of the size of the market units.

Issue - Rental units start out relatively small so the affordable units, at 80 percent of the square footage, can result in units too small to fit the required number of bedrooms/baths and required storage.

4. Affordable rental units must be owned all or in part by Boulder's housing authority, Boulder Housing Partners or a similar agency.

Issue - These non-profits must be willing and require both the funding and capacity to acquire off-site affordable units. They may need to turn to the city in the future for maintenance and capital improvement funding.

5. The provision of off-site units must be secured until they are completed.

Issue - The requirement for security creates an additional burden on the developer.

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[3] Ordinance uses the HUD low income limit to identify income targets, to simplify, we have translated the HUD incomes in to AMI numbers.
[4] Affordability gap is the difference between a home's market price and an affordable price.

6. Currently, there is no specific language in the IH ordinance concerning where or how off-site units may be provided. A provision in the IH Administrative Regulations states that off-site location and units are approved at the sole discretion of the city.

Issue - Further criteria are needed to guide approval of off-site locations. One development has provided affordable units off-site in two 100 percent affordable projects near each other in North Boulder. These projects raise questions and concerns about the number of affordable units in an off-site development and a possible future concentration of units in locations where vacant land is available and affordable.