MEMORANDUM

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Affordable Housing
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To: Ursula Luna-Reynosa, Community Development Director
City of Huntington Beach

From: Kathleen Head

Date: May 6, 2020

Subject: Inclusionary Housing :Policy & Implementation Recommendations

Keyser Marston Associates, Inc. (KMA) was engaged by the City of Huntington Beach (City) to assist in updating the requirements imposed by the Inclusionary Housing Ordinance. The update was undertaken for the following reasons:

1. To evaluate the impacts created by real estate economic changes and increases in the unmet need for affordable housing that have occurred since the Inclusionary Housing Ordinance requirements were last modified in 2011.

2. To modify the Inclusionary Housing requirements with the intention of achieving the following goals:

   a. To maximize the program's efficiency; and

   b. To match the requirements to the types of housing being developed.

KMA prepared the accompanying *Financial Analysis: Inclusionary Housing Ordinance Update* (Financial Analysis) to evaluate the economic characteristics of the Inclusionary Housing program as implemented since 2011. [1] The Financial Analysis serves as the foundation KMA used for creating a package of Inclusionary Housing policy and implementation recommendations.

[1] Capitalized terms used throughout this memorandum are defined in the Financial Analysis.

BACKGROUND

Based on the results of the Financial Analysis, KMA reached the following key conclusions:

1. Current Inclusionary Housing Requirements:

   a. The 10% moderate income requirement for ownership housing development continues to be supportable.

   b. The 10% low income requirement for rental apartment projects is supportable. There is no need to provide an option for moderate income units to be used as a substitute when the units are provided on site within a market rate project.

2. The maximum in-lieu fee amounts that can currently be supported on a financially feasible basis were estimated as follows:

Maximum Financially Feasible In-Lieu Fees		
	Ownership Housing	Rental Apartments
Inclusionary Housing Requirement	10% Moderate Income	10% Low Income
In-Lieu Fee Amounts		
Per Affordable Unit	$504,700	$332,000
Per Total Unit	$50,470	$33,200
Per Square Foot of Saleable/Leasable Area	$25.36	$35.80

Recommended Policy and Implementation Package

The Inclusionary Housing policy and implementation recommendations package consists of the following components:

1. The minimum residential project size that triggers an Inclusionary Housing obligation.

2. The income and affordability requirements that will be applied to ownership housing and rental apartment projects.

3. The covenant periods under which the income and affordability standards should be imposed for ownership housing and rental apartment projects.

4. To mitigate the financial impacts created by the imposition of Inclusionary Housing requirements options need to be provided that are tailored to the type of housing being developed. The following options are proposed to be offered under specified circumstances:

   a. On-site production;

   b. Off-site production;

   c. In-Lieu Fee Payment;

   d. Land Dedication; and

   e. Acquisition and rehabilitation of existing apartment units.

5. Implementation activities that should be undertaken by the City.

Case Studies

To assist the City in evaluating the proposed policy and implementation recommendations KMA prepared comparisons of the Inclusionary Housing options that could potentially be applied to a hypothetical project. Hypothetical projects are analyzed for an ownership housing project and a rental apartment project.

RECOMMENDED POLICY AND IMPLEMENTATION PACKAGE

Threshold Project Size

The majority of Inclusionary Housing programs in California include a threshold project size below which projects are not subject to the affordable housing production requirements. Common thresholds fall between three and 10 units. KMA recommends that the threshold project size be maintained at the three unit standard imposed by the City's existing Inclusionary Housing Ordinance.

It is important to understand that Inclusionary Housing requirements create a significant impact on smaller projects, because the financial impact created by the affordable housing requirement is spread over a small number of market rate units. The other issues to consider are:

1. Given the magnitude of the Affordability Gaps associated with ownership housing projects, small infill projects are disproportionately impacted by an affordable housing production requirement.[2]

2. Small rental apartment projects are often self-managed by owners that do not have experience owning and operating affordable housing units.

3. Monitoring and administering Inclusionary Units in small projects that are scattered throughout Huntington Beach will be a labor intensive obligation for City staff.

It is KMA's recommendation that projects with fewer than 100 units should be allowed to pay a fee in lieu of developing the required number of Inclusionary Housing units. At a 10% Inclusionary Housing requirement, a 100 unit project would generate a 10-unit Inclusionary Housing obligation. This is a sufficient number of affordable housing units to support the efficient management and administration of the units.

KMA recommends that a graduated in-lieu fee schedule continue to be offered in the updated Inclusionary Housing Ordinance. The recommended in-lieu fee payment structure is discussed further in the Inclusionary Housing production option section of this memorandum.

Income and Affordability Standards

An Inclusionary Housing program's income and affordability standards should be set at levels that do not constrain residential development. Based on the results of the Financial Analysis, KMA determined that the following Inclusionary Housing requirements can be supported.

[2] The Affordability Gap is defined as the difference between the achievable market rate sales prices or rents and the Affordable Sales Prices or Affordable Rents for the Inclusionary Housing units.

Ownership Housing Projects

Inclusionary Housing Requirement

KMA recommends that the City continue to designate moderate income units as the affordable housing type for ownership housing projects. Based on the Financial Analysis, KMA recommends that the affordable housing requirement remain at 10% of the units in an ownership housing project.

Affordable Sales Price Calculation Methodology

KMA strongly recommends that the City make modifications to the methodology used to estimate the Affordable Sales Prices. The specific issues relate to the methodology used to set the benchmark mortgage interest rate and the allowable range of home buyer down payments.

<u>Benchmark Mortgage Interest Rate</u>

In practice, the City has been using the lowest interest rate published during the preceding three month period. As an example, the rate being applied by the City in April 2020 is 2.46%. This rate is significantly lower than the rates for which typical moderate income home buyers will be able to qualify. Common reasons for this are:

1. Credit history and scores that do not fall within the exceptional level required to obtain the lowest interest rate available in the marketplace;

2. Back-end ratios that are often higher than the typical ratios applied in conventional lenders' underwriting standards for the lowest interest rate mortgages;

3. The lowest published interest rate is often a teaser rate that will ultimately adjust to a higher rate that will be unaffordable to the moderate income home buyer; and

4. There is a limited pool of mortgage lenders that are willing to provide loans on homes that are subject to long-term irrevocable resale restrictions. These lenders do not generally offer the lowest interest rates available in the marketplace.

The use of the lowest published interest rate is not required by the Inclusionary Housing Ordinance or by the Affordable Ownership Housing Regulations. The application of this metric generates extremely high Affordable Sales Prices, which can actually only be achieved by home buyers with the ability to make an extraordinarily large down payment.

KMA recommends that the City modify the policy being used to set the mortgage interest rate that is applied in the Affordable Sales Price calculations. KMA typically uses the Bankrate sitewide average annual percentage rate (APR) for 30-year fixed interest rate mortgages. In addition, KMA recommends that the benchmark interest rate be set on the on the first day of each calendar quarter.

Range of Allowable Home Buyer Down Payments

The Affordable Ownership Housing Regulations set the maximum home buyer down payment at 50% of the Affordable Sales Price. The high end of this range was established when it became apparent that typical moderate income home buyers could not qualify for the mortgage loans required to support the Affordable Sales Prices being set by the City.

The Inclusionary Housing program is intended to target home buyers that could otherwise not afford to purchase a home in Huntington Beach. Moderate income home buyers who have sufficient resources to fund a 50% down payment likely have other available opportunities to purchase a home.

KMA recommends that the down payment requirements be modified as follows:

1. The minimum home buyer down payment amount should be set at 5% of the Affordable Sales Price.

    a. This down payment amount must be provided from the home buyer's own funds.

    b. These funds cannot be provided using gifts or loans obtained by the home buyer.

2. The maximum down payment amount should be set at 20% of the Affordable Sales Price. Gift funds may be used for the down payment amount that falls between 5% and 20% of the Affordable Sales Price.

Rental Apartment Projects

The existing Inclusionary Housing Ordinance applies a 10% low income affordable housing requirement to rental apartment projects. However, the Inclusionary Housing Ordinance gives the City discretion to permit a developer to substitute moderate income units for the low income requirements.

Based on the City's RHNA targets, and the results of the Financial Analysis, KMA recommends that the updated Inclusionary Housing Ordinance should maintain the 10% low income housing requirement. The moderate income option should be eliminated.

A significant number of large scale apartment projects that have been developed in Huntington Beach have made use of the Government Code Sections 65915 – 65918 (Section 65915) density bonus. It should be assumed that developers will continue to use this approach as a means of mitigating the financial impacts created by an Inclusionary Housing requirement.

Covenant Periods

Ownership Housing Projects

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

Rental Apartment Projects

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

Options for Fulfilling Inclusionary Housing Obligations

On-Site Production of Inclusionary Housing Units

Ownership Housing Projects

By right, developers of ownership housing projects can fulfill the project's Inclusionary Housing obligations on site within the market rate project. Developers that wish to fulfill the Inclusionary Housing obligations on site should be provided with option to select one of the following fulfillment structures:

<u>Development of Affordable Ownership Housing Units</u>

The following standards mirror the Inclusionary Housing requirements currently being imposed by the City. These development parameters fall within the typical range for Inclusionary Housing programs throughout California, and KMA recommends that they be included in the updated Inclusionary Housing Ordinance.

1. The Inclusionary Housing obligation is set at 10% of the total number of units to be constructed on the site.
2. The following income and affordability standards are applied:
    a. The affordability requirement is set at the moderate income level.
    b. The Affordable Sales Prices must be calculated using the H&SC Section 50052.5 standards.
3. The affordable housing units must be built concurrently with the market rate project. The affordable units can be constructed in phases if the market rate project is being developed in phases.
4. The affordable housing units must comply with the following development scope requirements:
    a. The bedroom mix for the affordable units must be proportional to the bedroom mix of the market rate units. However, the affordable units may be smaller in square footage than the market rate units.

b. The exterior improvements for the affordable units must be comparable to the exterior improvements for the market rate units.

c. The interior improvements for the affordable units must meet the following standards:

i. The interior finished must be comparable to the base level interior finishes provided in the market rate units; and

ii. The appliance packages must be the same as the packages provided in the base level market rate units.

Development of Affordable Rental Apartments within an Ownership Housing Project

If the developer of an ownership housing project is willing to fulfill the project's Inclusionary Housing requirement with rental apartment units, KMA recommends that the following requirements be applied in the updated Inclusionary Housing Ordinance:

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

2. The developer of the market rate project can enter into an agreement with an affordable housing developer to construct, own and operate the affordable housing units:

    a. The affordable housing developer must have relevant recent experience, and must be approved by the City.

    b. The affordable housing developer may not request any financial assistance from the City.

3. The Inclusionary Housing obligation should be set at 10% of the total number of units to be constructed on the site.

4. The Inclusionary Housing obligation should be required to be fulfilled with rental apartment units that embody the following characteristics:

a. The threshold affordability standard is set at the low income level, but the developer should be provided with the discretion to fulfill the 10% requirement with very low income units.

b. The rents must calculated using the H&SC Section 50053 standards.

5. The bedroom mix should not be required to match the unit mix provided in the market rate ownership housing project. However, at least 40% of the Inclusionary Housing units should be required to include at least two bedrooms.

Rental Apartment Projects

KMA recommends that the updated Inclusionary Housing Ordinance apply the following standards to the on-site fulfillment of the Inclusionary Housing requirements imposed on rental apartment projects:

1. The Inclusionary Housing obligation should be set at 10% of the total number of units to be constructed on the site. [3]

2. The following income and affordability standards should be applied:

   a. The threshold affordability standard is set at the low income level, but the developer should be provided with the discretion to fulfill the requirement with very low income units.

   b. The Affordable Rents must be calculated using the H&SC Section 50053 standards.

3. The affordable housing units should be required to be constructed concurrently with the market rate project, and they must be dispersed throughout the project.

4. The affordable housing units should be required to comply with the following development scope requirements:

[3] If a developer chooses to use a Section 65915 density bonus the Inclusionary Housing obligation must be set at the lesser of 10% of the total number of units to be constructed on the site or 10% of the total number of units allowed by the site's base zoning standards.

a. The bedroom mix for the affordable units must be proportional to the bedroom mix of the market rate units. However, the affordable units may be smaller in square footage than the market rate units.

b. The interior improvements of the Inclusionary Housing units must comport with defined quality standards such as those applied by the Tax Credit program The market rate units in the project can include enhanced interior improvements.

Off-Site Production of Inclusionary Housing Units

KMA recommends that the updated Inclusionary Housing Ordinance allow a developer to fulfill the Inclusionary Housing obligations in an off-site location under the following conditions:

1. The development parcel should be required to be located within one mile of the market rate project that is subject to the Inclusionary Housing obligations.

2. The development must not create an over concentration of deed restricted affordable housing units in any specific neighborhood.[4]

3. Irrespective of the market rate project's tenure, the Inclusionary Housing obligation should be required to be fulfilled with rental apartment units.

4. The Inclusionary Housing obligation should be set at 15% of the total units included in the market rate project that generated the Inclusionary Housing requirements

5. The following income and affordability standards should be applied:

   a. The affordability standard should be set at the low income level, but developers should be provided with the discretion to fulfill the obligation with very low income units.

[4] Over concentration is defined as more than 50 covenanted very low or low income units within ¼ mile, or more than 200 such units within ½ mile of the of the proposed affordable housing site.

b. The Affordable Rents must be calculated using the H&SC Section 50053 standards.

6. Design, building quality and maintenance standards should be based on a defined standard such as the requirements imposed by the Tax Credit program.

7. The bedroom mix should not be required to match the unit mix provided in the market rate single family home project. However, at least 40% of the units should be required to include at least two bedrooms.

8. Under the following circumstances the developer of the market rate project can enter into an agreement with an affordable housing developer to construct, own and operate the affordable housing project:

   a. The affordable housing developer must have recent relevant experience, and be approved by the City.

   b. The affordable housing developer may not request any financial assistance from the City.

   c. The developer may apply to use the Section 65915 density bonus and the statutorily established number of incentives or concessions.

9. The affordable housing project should be required to be constructed prior to or concurrent with the market rate project that triggered the Inclusionary Housing obligation. If the market rate project is proposed to be developed in phases, the affordable housing project should be required to be developed along with the first phase of the market rate project.

In-Lieu Fee Payment Option

As currently implemented, the City allows developers of projects that include 30 or fewer units to pay a fee in lieu of producing affordable housing units. The in-lieu fee can also be paid to fulfill a fractional unit affordable housing obligation.

KMA recommends that the updated Inclusionary Housing Ordinance should encourage the use of an in-lieu fee payment options for premium priced ownership housing and rental apartment projects. The key advantages of this strategy are:

1. The City can target the use of the in-lieu fee revenue to projects undertaken by developers that have specific expertise in the development and operation of affordable housing projects.

2. The in-lieu fee revenues can be used as a leveraging source for dedicated affordable housing projects that have access to outside public funding sources. This leveraging creates a more cost-efficient way to achieve deeper affordability than can be supported by an Inclusionary Housing requirement alone.

In-Lieu Fee Payment Thresholds

KMA recommends that the in-lieu fee payment option be updated to allow developers to pay the fee by right in the following circumstances:

1. Single family home developments of any size should be provided with the option to pay an in-lieu fee.

2. Condominium/townhome ownership housing projects and rental apartment projects with fewer than 100 units should be allowed to pay an in-lieu fee.

3. An In-lieu fee payment option for a fractional affordable housing obligation should continue to be offered by the City.

4. For projects that do not meet the defined standards, the City Council should be provided with the discretion to allow an in-lieu fee to be paid if hardship circumstances are demonstrated.

In-Lieu Fee Schedules

The existing Inclusionary Housing Ordinance provides a graduated in-lieu fee schedule to reflect the fact that Inclusionary Housing requirements have a disproportionate impact on smaller projects. KMA recommends that a graduated in-lieu fee schedule continue to be offered in the updated Inclusionary Housing Ordinance.

It is KMA's opinion that an in-lieu fee measured against the square footages of the units corresponds more closely to the Affordability Gap associated with the market rate units being developed. As such, it is KMA's recommendation that the in-lieu fee schedules in the updated Inclusionary Housing Ordinance be based on the net saleable area for ownership housing projects and the net leasable area for rental apartment projects.

KMA created recommended in-lieu fee schedules that discount the in-lieu fee on a pro rata basis for projects with between three and 30 units. For projects with more than 30 units the in-lieu fee is a fixed dollar amount per square foot of saleable or leasable area.

Based on the results of the Financial Analysis, KMA recommends that the following in-lieu payment schedules be applied in the first year following the adoption of an updated Inclusionary Housing Ordinance:

Recommended In-Lieu Fee Schedules Per Square Foot of Net Saleable Area or Net Leasable Area					
# of Units	Ownership Housing	Rental Apartments	# of Units	Ownership Housing	Rental Apartments
3	$2.54	$3.58	17	$14.37	$20.29
4	$3.38	$4.77	18	$15.22	$21.48
5	$4.23	$5.97	19	$16.06	$22.67
6	$5.07	$7.16	20	$16.91	$23.87
7	$5.92	$8.35	21	$17.75	$25.06
8	$6.76	$9.55	22	$18.60	$26.25
9	$7.61	$10.74	23	$19.44	$27.45
10	$8.45	$11.93	24	$20.29	$28.64
11	$9.30	$13.13	25	$21.13	$29.83
12	$10.14	$14.32	26	$21.98	$31.03
13	$10.99	$15.51	27	$22.83	$32.22
14	$11.84	$16.71	28	$23.67	$33.41
15	$12.68	$17.90	29	$24.52	$34.61
16	$13.53	$19.09	30+	$25.36	$35.80

In-Lieu Payment Timing

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

Land Dedications

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

1. The developer must be willing to convey the property to the City at no cost.

2. The developer must provide evidence of the following when the land dedication proposal is submitted:

    a. The developer must have site control with lien-free title. Any encumbrances or easements that adversely impact the property's title must be disclosed and factored into the estimated value of the interests proposed to be conveyed to the City.

    b. The property cannot contain any hazardous materials at the time the land dedication proposal is submitted:

        i. The developer must disclose whether any hazardous materials were previously contained on the site; and

        ii. If hazardous materials were previously remediated, the developer must provide evidence that the cleanup was performed in accordance with applicable law.

    c. The property cannot have been improved with any residential use for at least five years prior to the submission of a land dedication proposal.

d. Payment in full of all property taxes and special taxes must have been made when the proposal is submitted, and again prior to conveyance of the property to the City.

3. The property must embody the following characteristics:

a. The property must be located within one-mile of the project that is subject to the Inclusionary Housing obligation.

b. The construction of affordable housing units on the property must not create an over concentration of low income housing in any specific neighborhood.

c. The number of units that must be able to be developed on a land dedication site should be set at 20% of the total units being constructed within the market rate project:

i. The site's existing General Plan and zoning standards must allow for a residential use at a density sufficient to allow for the requisite number of affordable units to be developed.

ii. The site must be suitable in terms of size, configuration, and physical characteristics to allow for the requisite number of affordable units to be developed on a cost efficient basis.

d. The property must be fully served by the necessary infrastructure prior to conveyance to the City.

4. It is the City's goal to convey dedicated properties to developers with experience developing affordable rental apartment projects targeted to very low income households. To assist the City in evaluating land dedication proposals, the developer should be required to submit the following documents:

a. A conceptual site plan and narrative description of a project that could be developed on the property.

b. A pro forma analysis that quantifies any financial gap associated with the identified development scope, and describes how this financial gap will be filled.

c. If a Section 65915 density bonus will be required, the terms of the necessary density bonus must be identified.

Prior to submitting a proposal to the City Council for consideration, the City staff should independently evaluate the information submitted by the developer. Based on that review the City should determine whether the proposal meets the threshold standards proposed to be included in the updated Inclusionary Housing Ordinance.

Acquisition and Rehabilitation Projects

The Inclusionary Housing Ordinance is one tool the City is using to assist in meeting its RHNA targets. The only way that the acquisition and rehabilitation of existing units can be used to obtain RHNA credit is if the following conditions are met:

1. The project(s) must be identified in the City's Housing Element; and

2. The units must be in need of substantial rehabilitation as defined by H&SC Section 33413 (2) (A) (iv).

For projects that meet both of these requirements, the City Council should have the discretion, but not the requirement, to approve a developer's acquisition and rehabilitation proposal. KMA recommends that this option only be approved if the proposed acquisition and rehabilitation project provides more affordable units at deeper affordability than would be achieved under any of the other Inclusionary Housing options discussed in this memorandum.

The additional threshold requirements that should be imposed on acquisition and rehabilitation projects are:

1. The project must meet one of the following criteria:

   a. The project includes affordable units that are at risk of being converted to market rate units within a five year period; or

   b. The project is a motel that can be adaptively reused as residential units.

2. The Inclusionary Housing requirement is equal to at least 20% of the units in the project that trigged the Inclusionary Housing obligation:

   a. The rents charged for the Inclusionary Housing units must be set at the lesser of the H&SC 50053 rents or an at least 10% discount from the achievable market rents for the units.

   b. If there are more units in the acquisition and rehabilitation project than are required to fulfill the Inclusionary Housing requirement, those units may be rented at unrestricted market rate rents.

3. Any very low or low income households currently residing in the project must be provided with the following benefits:

   a. They must be allowed to stay in place following the acquisition and rehabilitation.

   b. The rents charged to these tenants must comport with the requirements imposed by H&SC Section 50053 for the tenant's income level.

   c. Any temporary relocation costs incurred during the rehabilitation period must be paid for by the developer.

   d. These tenants can only be evicted on a just cause basis.

Implementation Recommendations

As part of the implementation process for the updated Inclusionary Housing Ordinance, the City should take the following actions:

Section 65915 Density Bonus

The City's Section 65915 density bonus ordinance does not currently include all of the amendments the State Legislature has made between 2006 and 2019. Given that the Section 65915 density bonus is intended to reduce the financial impact created by the imposition of Inclusionary Housing requirements, KMA recommends that the City update Zoning Code Title 23, Chapter 230, Article I, Section 230.14 to reflect the current requirements.

Affordable Housing Regulations

The following Inclusionary Housing Ordinance regulations documents should be updated:

1. Affordable Ownership Housing Regulations: Developer Requirements;

2. Affordable Ownership Housing Regulations: Owner Requirements; and

3. Affordable Rental Housing Regulations.

Inclusionary Housing Program Updates

The Inclusionary Housing program should be updated at regular intervals:

1. The entire program should be re-evaluated at least every five years.

2. To allow in-lieu fees to keep pace with changes in the market place during the intervening periods, the in-lieu fees should continue to be adjusted each year based on the percentage change in new home prices in Orange County as published annually by the Real Estate Research Council (RERC).

Implementation Activities

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

CASE STUDIES

Background

The following section of this memorandum describes case studies for a hypothetical ownership housing project and a hypothetical rental apartment project. Both projects include 250 units, but they are assumed to be developed at different densities and with different unit mixes.

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

Fulfillment Options that Vary Between Ownership Housing and Rental Apartments

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

1. Production of the Inclusionary Housing units on site within the market rate project; and

2. A fee payment in lieu of producing affordable housing units.

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

1. The development scope assumptions are described.

2. The requirements associated with providing the Inclusionary Housing within the market rate projects are detailed.

3. An in-lieu fee payment estimate is provided for the hypothetical development.

Standardized Fulfillment Options

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

1. Production of the Inclusionary Housing Units in an off-site location;

2. Dedication of land to the City in lieu of producing affordable housing units; and

3. Acquisition and rehabilitation of existing units.

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

1. The development scope assumptions that guide the Inclusionary Housing requirements;

2. The affordability requirements associated with each option; and

3. The unit mix standards applied to each option are presented.

Ownership Housing Project: On-Site Production and In-Lieu Fee Options

Development Scope Assumptions – Ownership Housing Project

The development scope used the ownership housing hypothetical are:

1. The 250 unit project is developed on a 12.5-site. This represents a density of 20 units per acre.

2. The Inclusionary Housing obligation is equal to 25 units, which represents 10% of the units in the market rate project.

3. The project is developed in five phases.

4. The unit mix is detailed in the following table:

Unit Mix		
Number of Bedrooms	Number of Units	Square Feet Per Unit
3	50	1,900
3	75	2,300
4	50	2,600
4	75	3,000
Total	250	622,500

On-Site Production Options – Ownership Housing Project

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

The two alternatives can be described as follows:

On-Site Production of Affordable Ownership Units

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

1. The Inclusionary Housing requirement is set at 10% of the total number of units to be constructed on the site. This equates to 25 units out of the 250 proposed units.

2. The income restriction is set at the moderate income level.

3. The bedroom mix required to be applied to the Inclusionary Housing units is based on pro rata shares of the three- and four-bedroom units in the market rate project, allocated to the smaller of the unit types in each bedroom category. For the hypothetical project, the Inclusionary Housing units are distributed as follows:

    a. 13 three-bedroom units with saleable area of 1,900 square feet; and

    b. 12 four-bedroom units with saleable area of 2,600 square feet.

4. The project is assumed to be developed in five phases. Assuming the 250 units are divided equally across the five phases, five affordable units must be constructed in each phase.

On-Site Production of Affordable Rental Apartment Units

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

1. The Inclusionary Housing requirement is set at 10% of the total number of units to be constructed on the site. This equates to 25 units out of the 250 proposed units.

2. The income restriction is set at the low income level.

3. The affordable units developed on the separate parcel are not required to match the unit mix provided in the market rate project. Instead, the following requirements are applied in this hypothetical case study:

    a. A maximum of 15 units (60%) can be studio or one-bedroom units; and

    b. At least 10 units (40%) must include two or more bedrooms.

4. All 25 affordable rental apartment units must be constructed prior to or concurrent with the construction of the first phase of the market rate ownership housing project.

In-Lieu Fee Payment Option

For the hypothetical 250 unit ownership housing project, a developer can use the in-lieu fee option under the following conditions:

1. A project that consists of single family homes can select the in-lieu fee option by right.

2. A condominium or townhome project would be required to obtain City Council approval in order to be allowed to use the in-lieu fee option.[5]

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

1. The total saleable area of the 250 unit market rate project is 622,500 square feet.

2. The in-lieu fee for projects that include 30 or more units is $25.36 per square foot of saleable area.

[5] A condominium or townhome project with up to 100 units can select the in-lieu fee option by right.

3. The resulting total in-lieu fee is $15.8 million, which equates to approximately $63,151 per unit in the market rate project.

Rental Apartment Project: On-Site Production and In-Lieu Fee Options

The development scope used the rental apartment project hypothetical are:

1. The 250 unit project is developed on a five acre-site. This represents a density of 50 units per acre.

2. The Inclusionary Housing obligation is equal to 25 units, which represents 10% of the units in the market rate project.

3. The unit mix is presented in the following table:

Unit Mix		
Number of Bedrooms	Number of Units	Square Feet Per Unit
Studio	35	600
1	120	800
2	75	1,000
3	20	1,200
Total	250	216,000

On-Site Production of Affordable Rental Apartment Units

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

1. At a 10% Inclusionary Housing requirement, 25 affordable units must be provided.

2. The income restriction is set at the low income level.

3. To match the distribution of the bedroom types included in the market rate project, the affordable units must be provided in the following mix:

Number of Bedrooms	Number of Units
Studio	4
1	12
2	8
3	1
Total	25

4. The affordable units must be dispersed throughout the market rate project and developed concurrently with the market rate project.

In-Lieu Fee Payment Option

Under the recommended structure, a 250 unit rental apartment project would not be allowed to pay a fee to fulfill the Inclusionary Housing obligation. However, if the developer can prove a financial hardship, the City Council has the discretion to approve the payment of an in lieu fee.

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

1. The total leasable area of the 250 unit market rate project is 216,000 square feet.

2. The in-lieu fee for projects that include 30 or more units is $35.80 per square foot of leasable area.

3. The resulting total in-lieu fee is $7.7 million, which equates to approximately $30,900 per unit in the market rate project.

Other Inclusionary Housing Obligation Fulfillment Options

Each of the three remaining Inclusionary Housing obligation fulfillment options includes the following common assumptions:

1. The market rate project that triggered the Inclusionary Housing requirement includes 250 units; and

2. The Inclusionary Housing obligation must be fulfilled with rental apartment units.

Off-Site Production Option

The City has approval rights over the following:

1. The development site proposed to be used; and

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

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

1. The Inclusionary Housing requirement is set at 15% of the units included in the market rate project.

2. At 250 units the market rate project generates a requirement for 38 affordable units.

3. The affordability standard is set at the low income level.

4. The affordable units are not required to adhere to the bedroom mix included in the market rate project. The standards that are imposed on the off-site development option are:

   a. No more than 60% of the units (23) can be studio or one-bedroom units; and

   b. At least 40% of the units (15) must include two or more bedrooms.

5. The Inclusionary Housing obligation must be fulfilled prior to or concurrent with the first phase of the market rate development.

Land Dedication Option

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

1. The Inclusionary Housing obligation is set at 20% of the units being constructed in the market rate project.
2. A 50 unit affordable housing unit requirement is imposed on the hypothetical 250 unit market rate project.
3. At an assumed allowable density of 50 units per acre, the dedicated site must include at least 43,560 square feet of land area.
4. The affordability standard is set at the very low income level.
5. The unit mix requirements are:
    a. No more than 50% of the units can be studio or one-bedroom units; and
    b. No fewer than 50% of the units must include two or more bedrooms.
6. The developer must submit a conceptual plan and a pro forma analysis to demonstrate that a 50 unit project targeted to very low income households will be feasible with no financial contribution from the City.

Acquisition and Rehabilitation Option

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

1. The Inclusionary Housing requirement is set at 20% of the units being constructed in the market rate project.
2. To fulfill the affordable housing requirement a developer would need to acquire and rehabilitate existing projects that include a total of at least 50 units.
3. The affordability standard is set at the very low income level.

4. The rehabilitation scope must comport with the following requirements:

   a. The improvements must have a value equal to at least 25% of the after rehabilitation value of the units, which includes the value of the land.[6]

   b. It is required that at least 50% of the acquired and rehabilitated units include at least two bedrooms. This may require reconfiguration and conversion of some units in the projects that are acquired.

SUMMARY

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

It is the City's goal to update the Inclusionary Housing Ordinance in ways that balance the interests of property owners and developers against the public benefits associated with increasing the inventory of affordable housing units in the community. To that end, KMA identified financially feasible Inclusionary Housing production requirements and provided a mix of alternative methods for fulfilling the requirements.

[6] H&SC Section 33413 (2) (a) (iv).

KEYSER MARSTON ASSOCIATES™

FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE

Prepared for:

City of Huntington Beach

Prepared by:

Keyser Marston Associates, Inc.

May 6, 2020

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I. OVERVIEW

The City of Huntington Beach (City) has imposed Inclusionary Housing requirements on residential development since the early 1990's. During the intervening period the City Council has taken the following actions related to the Inclusionary Housing policy:

1. In October 2005 the City Council adopted an Inclusionary Housing Ordinance to codify the affordable housing policy. [1] The key requirements imposed by the Inclusionary Housing Ordinance can be summarized as follows:

    a. Projects with three or more units are subject to a 10% Inclusionary Housing requirement:

        i. Projects with between three and 10 units were allowed to pay a fee in lieu of producing affordable units.

        ii. Under specified circumstances the affordable housing requirements could be fulfilled in off-site locations with new development or the acquisition and rehabilitation of existing units.

    b. The following income standards were applied:

        i. For ownership housing projects the requirement was set at very low, low or median income at the City's discretion; and

        ii. For rental apartment projects the requirement was set at very low or low income at the City's discretion

    c. The covenant period was set at 60 years for both ownership housing and rental apartment projects.

[1] The Inclusionary Housing Ordinance is codified in Zoning Code Title 23, Chapter 230, Article I, Section 230.26.

2. In July 2009 the City Council approved the following changes to the Inclusionary Housing Ordinance:[2]

   a. The in-lieu fee payment option was expanded to include projects with up to 30 units

   b. The household income limits were modified as follows:

      i. For ownership housing projects the requirement was set at the moderate income level; and

      ii. For rental apartment projects the requirement was set at the low income level. However, with City approval affordable units built within the market rate projects can fulfill the obligation with moderate income units.

   c. The affordable units must have a bedroom mix that is proportionate to the market rate unit mix. However, the smallest units of each bedroom type can be used.

   d. In August 2011 the City published the following regulations that detail the Inclusionary Housing Ordinance requirements:

      i. Affordable Ownership Housing Regulations: Developer Requirements;

      ii. Affordable Ownership Housing Regulations: Owner Requirements; and

      iii. Affordable Rental Apartment Regulations.

[2] The Inclusionary Housing Ordinance has not been amended to reflect the approved changes. However, in practice, the City has been implementing the changes.

The City engaged Keyser Marston Associates, Inc. (KMA) to assist in updating the requirements imposed by the Inclusionary Housing Ordinance. This update is being undertaken because conditions have changed since the Inclusionary Housing Ordinance requirements were last modified in 2011. The following *Financial Analysis: Inclusionary Housing Ordinance Update* (Financial Analysis) evaluates the following topics:

1. The appropriateness of the 10% affordable housing requirement;

2. The fee amounts that can be supported for projects that are permitted to pay a fee in lieu of producing affordable housing; and

3. Alternative means of fulfilling the affordable housing requirements imposed by the Inclusionary Housing Ordinance.

This Overview section describes the basic parameters that guide Inclusionary Housing programs throughout California.

A. Key Court Cases

It is important to review the key legal cases and State legislation that guide the implementation of Inclusionary Housing programs. A chronological summary of the relevant issues follows.

Palmer Case

In 2009, the California Court of Appeal ruled in *Palmer/Sixth Street Properties L.P. v. City of Los Angeles,* 175 Cal. App. 4th 1396 (*Palmer*), that the local affordable housing requirements being imposed by the City of Los Angeles violated the Costa-Hawkins Rental Housing Act (Costa-Hawkins). Specifically, Costa-Hawkins allows landlords to set the initial monthly rent for a new unit, and then to increase the monthly rent to the market level each time a unit is vacated. The Court found that the imposition of long-term income and affordability restrictions on rental residential units is a violation of this provision.

It is commonly believed that the *Palmer* ruling prohibited jurisdictions from requiring developers to construct affordable rental apartment units as a part of their Inclusionary Housing program. In an effort to comply with *Palmer*, jurisdictions generally took one of the following actions:

1. The jurisdiction eliminated the requirement that market rate rental apartment projects provide affordable rental apartment units; or

2. The jurisdiction replaced affordable housing production models with a linkage or impact fee methodology; or

3. The jurisdiction imposed affordable housing requirements as part of negotiated Development Agreements for rental apartment projects.

San Jose Case

In 2015, the California Supreme Court ruled in *California Building Industry Association v. City of San Jose,* 61 Cal 4th 435 (*San Jose*) that Inclusionary Housing programs should be viewed as use restrictions that are a valid exercise of a jurisdiction's zoning powers. Specifically, the Court found that Inclusionary Housing requirements are a planning tool rather than an exaction. This is interpreted to mean that an in-lieu fee payment option that is included in an Inclusionary Housing program, that includes an affordable housing production requirement, is not subject to the AB 1600 nexus requirements imposed by the "Mitigation Fee Act".[3]

Price controls imposed by Inclusionary Housing programs must meet the following criteria:

1. The requirements cannot be "Confiscatory"; and

2. The requirements cannot deprive a property owner of a fair and reasonable return on their investment.

[3] The Mitigation Fee Act is codified in California Government Code §66000 et seq.

The *San Jose* ruling that Inclusionary Housing programs are not an exaction applies to both ownership housing and rental apartment development. However, the *San Jose* case did not overturn the limitations *Palmer* imposed on Inclusionary Housing programs for rental apartment projects.

The *San Jose* case is also relevant to rental apartment projects, because former Governor Brown publicly stated that he would not sign a "*Palmer Fix*" bill unless and until the California Supreme Court ruled in favor of the City of San Jose. As such, the *San Jose* ruling opened the door for the subsequent passage and adoption of Assembly Bill (AB) 1505 in September 2017.

B. Legislation: AB 1505

AB 1505, which is otherwise known as the "*Palmer* Fix", was signed into law on September 29, 2017. AB 1505 amends Section 65850 of the California Government Code and adds Section 65850.01. This legislation provides jurisdictions with the ability to adopt programs that impose affordable housing requirements on rental apartment projects.

Role of the California Department of Housing and Community Development (HCD)

Section 65850.01 does not place a cap on the percentage of units that can be subject to income and affordability restrictions. However, Section 65850.01 (a) gives HCD the authority to review the restrictions imposed by an Inclusionary Housing program on rental apartment developments if it requires that more than 15% of the units to be restricted to households earning less than 80% of the area median income (AMI), and if one of the following conditions applies:

1. The jurisdiction has failed to meet at least 75% of its Regional Housing Needs Assessment (RHNA) allocation for above moderate income units. This test is measured on a pro-rated basis over the planning period, which is set at a minimum of five years; or

2. HCD finds that the jurisdiction has not submitted their housing element report for at least two consecutive years.

As of December 31, 2019, the City has exceeded the RHNA goal for above moderate income housing. The City received Housing Element approval from HCD in March 2020, but prior to that HCD had deemed the City out of compliance since 2015. Since the City has not submitted their housing element report for at least two consecutive years HCD has the right to require an economic feasibility study if more than 15% of rental apartment units in a project are required to be restricted at less than 80% of AMI.

It is likely that this Financial Analysis meets the economic feasibility study standards defined in Section 65850.01 (b). However, if the City chooses to impose a greater than 15% affordability requirement and/or deeper affordability standards on rental apartment projects, HCD can intervene in the Inclusionary Housing Ordinance update process. This could extend and complicate the approval process for updates to the Inclusionary Housing Ordinance being considered by the City.

Additional AB 1505 Requirements

Section 65850 (g) requires jurisdictions to provide alternative means of fulfilling the affordable housing requirements imposed on rental apartment projects by an Inclusionary Housing program. Options that can be provided to developers include, but are not limited to:

1. Off-site construction of affordable units;
2. Payment of a fee in-lieu of producing affordable housing units;
3. Land dedication; and
4. The acquisition and rehabilitation of existing units.

C. Inclusionary Housing Program Characteristics

Over 170 jurisdictions in California currently include an Inclusionary Housing program as a component in their overall affordable housing strategy. While the unifying foundation of these programs is the objective to attract affordable housing development, the characteristics of these programs vary widely from jurisdiction-to-jurisdiction.

To assist the City in evaluating options for updating the Inclusionary Housing Ordinance it is useful to identify the elements that are typically included in Inclusionary Housing programs being implemented in California jurisdictions. To that end, KMA compiled information on 64 Inclusionary Housing programs being implemented throughout California. The survey information is presented in Attachment 1 and is summarized in the following sections of this Financial Analysis.

1. In California, the majority of Inclusionary Housing programs include a threshold project size below which projects are not subject to the affordable housing requirements. Common thresholds fall between three and 10 units. The average threshold project size found in the program survey is eight units.

2. The income and affordability standards imposed by Inclusionary Housing programs vary widely throughout California. The majority of programs have established standards in the range of 10% to 20% of the units in projects that will be subject to the requirements. However, the following policy variations are commonly found:

    a. The threshold standards are varied as a reflection of the depth of the affordability being provided.

    b. Inclusionary Housing requirements have a disproportionate impact on smaller projects, because there are fewer market rate units available to spread the impact created by the income and affordability standards. A sliding scale requirement is sometimes used to mitigate these impacts.

c. The length of the covenant period imposed on Inclusionary Housing units varies from jurisdiction-to-jurisdiction. The California Health and Safety Code (H&SC) Section 33413 standards of 45 years for ownership housing units and 55 years for rental apartment units is commonly used. However, both shorter and longer covenant periods are imposed throughout Inclusionary Housing programs in California.

Inclusionary Housing programs focus on the production of affordable housing units by imposing specific affordable housing requirements on new development. To comply with the findings in the *San Jose* case, and the requirements imposed by Sections 65850 and 65850.01, Inclusionary Housing programs must offer developers a range of options for fulfilling the affordable housing requirements. The most common options offered to developers are:

1. Construction of a defined percentage of income restricted units within new market rate residential projects;

2. Construction of a defined percentage of income restricted units in a project located in an off-site location;

3. Payment of a fee in lieu of producing affordable housing units in which the revenues will subsequently be used by the jurisdiction to assist in the development of affordable housing units within the community;

4. The dedication of land to the jurisdiction that is appropriate for the development of affordable housing; and

5. The acquisition and rehabilitation of existing units.

The requirements imposed by the City's existing Inclusionary Housing Ordinance can be considered typical within the context of the surveyed programs. As such, the focus of this KMA evaluation is on updating the Inclusionary Housing Ordinance to reflect current market and financial conditions.

D. State Density Bonus and Inclusionary Housing Requirements

A tool that is commonly used to reduce the financial impact associated with the imposition of Inclusionary Housing requirements is the density bonus provided by California Government Code Sections 65915-65918 (Section 65915). Section 65915 requires jurisdictions to provide density bonuses based on a sliding scale ranging from 5% to 35% depending on the magnitude of the income restrictions being imposed.

In July 2013 the First District Court of Appeal held that jurisdictions must agree to count the affordable units used to fulfill the Section 65915 density bonus requirements towards the Inclusionary Housing requirements that will be imposed on a project.[4] Based on that ruling, a developer must be allowed to use the same affordable units to fulfill both the Inclusionary Housing requirements and the Section 65915 requirements. However, in order to exercise this option, the developer must apply the more stringent of the two programs' requirements.

The Section 65915 density bonus can act to materially reduce the financial impacts created by Inclusionary Housing requirements. For that reason, the City should recognize that when Inclusionary Housing requirements are imposed it is highly likely that many developers will make use of Section 65915 density bonuses. It is also important to understand that the City is required to grant a developer's request for the statutorily established density bonus along with the requisite number of concessions and incentives, as well as any necessary development standards reductions or waivers.[5]

Section 65915 requires the City to adopt an ordinance that specifies how it will comply with the State mandated density bonus requirements. The City adopted a density bonus ordinance in 2005 and it has amended the ordinance four times.[6] However, the City's density bonus

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[4] *Latinos Unidos del Valle de Napa y Solano v. County of Napa,* 217 Cal. App. 4th 1160 (*Napa*).
[5] Section 65915 (d) (1) identifies three conditions under which requested incentives or concessions can be denied. However, this does not relieve the City of the obligation to grant the number of incentives or concessions that the project is entitled to under Section 65915 (d) (2).
[6] The density bonus ordinance is codified in Zoning Code Title 23, Chapter 230, Article I, Section 230.14.

ordinance has not been updated to reflect several modifications that have been made by the State Legislature to Section 65915 over time. Until such time as the modifications are amended into the City's density bonus ordinance, State law will automatically prevail over any inconsistencies between State law and the City's ordinance.

II. SUPPORTABLE INCLUSIONARY HOUSING REQUIREMENTS

As discussed previously, the court in the *San Jose* case found that the imposition of Inclusionary Housing requirements is a valid exercise of the City's zoning powers rather than an exaction. Sections 65850 and 65850.01 amended the California Government Code to expressly allow Inclusionary Housing requirements to be imposed on rental apartment projects.

It is important for the City to consider the following caveats when updating the Inclusionary Housing Ordinance

1. Inclusionary Housing requirements cannot be confiscatory or deprive an owner of a fair and reasonable return. However, recognizing that the courts have not defined these terms, the City has some discretion in establishing evaluation parameters.

2. California Government Code Section 65583 (a) (Section 65583 (a)) requires the City to analyze potential and actual constraints being placed on the development of housing. Within that context, it is important to recognize that the requirements imposed by the Inclusionary Housing Ordinance can only be expected to fulfill a small portion of the unmet need for affordable housing in Huntington Beach.

As mentioned previously, the City has been imposing Inclusionary Housing requirements on residential development since the early 1990's. As such, residential developers and owners of residentially zoned land are fully aware of the financial impacts created by the affordable housing requirements. Given that building permits were obtained for 2,915 housing units between 2013 and 2018 it can safely be concluded that to date the Inclusionary Housing Ordinance has not acted as a constraint to development.

The key factors that should be considered in updating the Inclusionary Housing Ordinance are:

1. The requirements should balance the interests of property owners and developers against the public benefit created by the production of income restricted units; and

2. The Inclusionary Housing requirements cannot be confiscatory or deprive an owner of a fair and reasonable return on their investment.

III. METHODOLOGY

The purpose of this analysis is to assist the City in updating the Inclusionary Housing Ordinance. The evaluation is comprised of the following steps:

A. Inclusionary Housing Requirements that are Currently Being Imposed

Basic Requirements

1. The Inclusionary Housing requirements apply to residential projects that include three or more units.

2. The affordable housing units must be built concurrently with the market rate project. The units can be constructed in phases if the market rate project is being developed in phases.

3. The affordable housing units must comply with the following development scope requirements:

    a. The bedroom mix for the affordable units must be proportional to the bedroom mix of the market rate units. However, the affordable units may be smaller in square footage than the market rate units.

    b. The exterior improvements for the affordable units must be comparable to the exterior improvements for the market rate units.

c. The interior improvements for the affordable units must be comparable to the base level interior finishes provided in the market rate units.

Income and Affordability Covenants

The Inclusionary Housing requirement is set at 10% of the units in ownership housing and rental apartment development projects. The specific income and affordability standards that are currently being applied are as follows:

Ownership Housing Projects:

1. The affordable units must be sold to moderate income households.

2. The H&SC Section 50052.5 calculation methodology is used to set the "Affordable Sales Prices".

3. The covenant period is set at one cumulative total of 45 years. Within that one 45-year period the home must be sold and resold at an Affordable Sales Price to moderate income households.

Rental Apartment Projects:

1. Under the current policy, the affordable units are to be rented to low income households. However, moderate income units may be allowed to be used to fulfill the requirement if the units are provided on site within the market rate project.

2. The H&SC Section 50053 calculation methodology is used to establish the "Affordable Rents" each year.

3. The covenant period is set at 55 years.

Alternative Inclusionary Housing Requirement Fulfillment Options

Developers currently have the option to fulfill the Inclusionary Housing requirements in the following ways:

In-Lieu Fees

An in-lieu fee can be paid to fulfill a fractional affordable unit obligation. An in-lieu fee can also be paid by projects with between three and 30 units. Restrictions applied to the in-lieu fee are:

1. The City Council establishes the in-lieu fee schedule each year.

2. The in-lieu fee must be paid when the building permits for the project are issued.

3. The in-lieu fee revenue is deposited into the "Inclusionary Housing Trust Fund". The City must allocate at least 20% of these funds to assist very low income households, and at least 50% of the total funds must be used to assist very low and low income households.

Off-Site Affordable Housing Production

The Inclusionary Housing requirements can currently be fulfilled in off-site locations under the following criteria:

1. Newly constructed units must fulfill the same development scope requirements that are applied to affordable units constructed within the market rate project.

2. The affordable units can be provided in existing projects that meet the following criteria:

    a. The units must not be subject to existing income and affordability covenants unless the units are at risk of being converted to unrestricted market rents.

    b. The units must require substantial rehabilitation, which is defined as one-third of the value of the existing improvements, excluding land.

3. Mobile homes can be used to fulfill the affordable housing requirement.

B. Regional Housing Needs Assessment (RHNA)

To assist in creating updates to the existing Inclusionary Housing Ordinance it is useful to identify the composition of the City's unmet need for housing. One measurement is the RHNA, which is used as a tool in the Housing Element process. The most recent RHNA covers the period between 2013 and 2021. At the end of 2019 the City's progress towards fulfilling the defined RHNA targets is presented in the following table:

City of Huntington Beach RHNA Information 2013 – 2021
Progress as of December 31, 2019

				Unfilled RHNA Targets	
Income Category	RHNA Targets	Building Permits Issued	Entitled Units	Total	%
Very Low	313	50	0	263	84%
Low	220	47	1	172	78%
Moderate	248	274	9	(35)	0%
Above Moderate	572	2,574	266	(2,649)	0%
Totals [7]	1,353	2,945	276	435	82%

As can be seen in the preceding table, the above moderate income target has been exceeded by a significant margin, and 35 more units were produced than the current moderate income target. [8] This indicates that the Inclusionary Housing Ordinance should focus on the attraction of very low and low income units. However, this goal needs to be balanced against the

[7] The Total Unfilled RHNA Target and the Percentage of Remaining RHNA Target calculations exclude the excess number of moderate and above-moderate income units that have been permitted.
[8] The Southern California Association of Governments (SCAG) staff recommended RHNA allocation for 2021 - 2029 totals 13,337 units. No credit will be provided for units produced in excess of the 2013 - 2021 targets.

requirement that the Inclusionary Housing Ordinance cannot be structured in a way that places an onerous financial burden on the developers of market rate housing.

Recognizing that the vast majority of housing that has been constructed in Huntington Beach over the past five years has been premium priced ownership housing units and rental apartments, it may be advantageous to update the Inclusionary Housing Ordinance requirements to encourage off-site production and in-lieu fee payment options. The key advantages of this strategy are:

1. The affordable housing units can be developed by developers that have specific expertise in the development and operation of affordable housing projects.

2. Dedicated affordable housing projects have access to public funding sources that provide a more cost-efficient way to achieve deeper affordability than can be supported by an Inclusionary Housing requirement. A representative sample of programs that are targeted to dedicated affordable housing projects are:

    a. Low and Moderate Income Housing Asset Funds (LMIHAF) that are under the control of the City, which acts as the Housing Successor to the former Huntington Beach Redevelopment Agency;

    b. HOME Program funds that are awarded to the City by the United States Department of Housing and Urban Development (HUD);

    c. The federal and state Low-Income Housing Tax Credits (Tax Credits) offered under Internal Revenue Code Section 42;

    d. State funding sources such as the Affordable Housing and Sustainable Communities (AHSC) Program; and

    e. The funds allocated to the City by HCD under the Permanent Local Housing Allocation (PLHA) for Senate Bill 2 (Chapter 364, Statutes of 2017).

C. Financial Analysis Organization

The financial analyses are organized as follows:

Step	Analysis
1	Creation of residential prototypes that are representative of new market rate development in Huntington Beach.
2	A survey of representative projects to estimate the achievable market rate sales prices and rents for the prototype units.
3	Estimation of the Affordable Sales Prices and Affordable Rents.
4	An evaluation of the existing 10% Inclusionary Housing requirement: a. For ownership housing projects KMA prepared a pro forma analysis for a prototype condominium project that includes a 10% moderate income requirement and a pro forma analysis for the same project assuming that the 2019 in-lieu fee amount is paid. b. For rental projects KMA prepared pro forma analyses for a prototype rental apartment project under three alternative income and affordability standards.
5	Projection of the in-lieu fees per square foot of net saleable or leasable area that can be supported.

IV. OWNERSHIP HOUSING ANALYSIS

The Inclusionary Housing Ordinance requires 10% of the units in ownership housing projects to be allocated to moderate income households. Imposing a moderate income requirement on ownership housing units reflects the fact that these households are likely to have more discretionary income to devote to the ongoing costs associated with home ownership than that of lower income households.

Recent new ownership housing development in Huntington Beach has been focused largely on detached single family home projects, with scattered development of condominiums and townhomes.[9] However, for the following reasons the prototype ownership housing project created by KMA for the pro forma analysis is a condominium project:

1. For single family homes, the weighted average gap between the market rate price and the Affordable Sales Price for a moderate income household is approximately $1.74 million.[10]

2. It is clear that exercising an option to pay an in-lieu fee or to provide off-site affordable housing units could be structured to produce more affordable units at a deeper affordability level than fulfilling the Inclusionary Housing requirement within a market rate single family home project.

3. Higher density condominium projects are currently being proposed for development in Huntington Beach. The gap between the market rate prices and the Affordable Sales Prices for this product type is significantly smaller than the gap exhibited by single family homes. Therefore, the potential for fulfilling Inclusionary Housing obligations on site merits evaluation.

A. Supporting Documents: Ownership Housing Analysis

The documents that support the ownership housing analysis are presented in Attachment 2. The following condominium pro forma analyses are used to evaluate the existing moderate income affordable housing production requirements and to estimate the supportable in-lieu fees per square foot of net saleable building area. The analyses are organized as follows:

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[9] To compile sufficient data the home sales survey for condominiums and townhomes had to be extended to projects built as early as 1990. Comparatively, it was possible to limit the survey of single family home sales to projects constructed after 2010.

[10] See Attachment 2 – Appendix B – Exhibit II.

Financial Analysis – Ownership Housing	
Appendix A	Condominium Analyses
Appendix B	Affordability Analyses
Appendix C	Home Sales Survey

B. Condominium Prototype

KMA created a prototype based on a review of condominium projects proposed for development and existing condominium projects in Huntington Beach. The key characteristics of the condominium prototype used in the pro forma analyses are:

Condominium Prototype	
Site Area (Square Feet)	43,560
Total Number of Units	40
Density (Units Per Acre)	40
Unit Mix	
Two-Bedroom Units	20
Three-Bedroom Units	10
Four-Bedroom Units	10
Average Unit Sizes (Square Feet)	
Two-Bedroom Units	1,530
Three-Bedroom Units	1,900
Four-Bedroom Units	3,000
Parking	
Total Number of Spaces	110
Parking Spaces Per Unit [11]	2.75
Parking Type	Subterranean

[11] Based on the citywide parking standards of 2.0 spaces for two-bedroom units; 2.5 spaces for three- and four-bedroom units; and .5 guest spaces per unit.

C. Projected Market Rate Sales Prices

It is important to note that the prototype analysis is intended to reflect average or typical ownership housing projects rather than any specific project. It should be expected that specific projects will vary to some degree from the prototype.

To assist in projecting the achievable market rate sales prices, KMA compiled sales data for condominiums sold in Huntington Beach between March 2019 and March 2020 (Attachment 2 – Appendix C). This information is used to establish the average sales price per square foot of saleable area for two-, three- and four-bedroom condominium units.

Based on the results of the surveys, KMA estimated the market rate sales prices as follows:

Projected Market Rate Sales Prices – Ownership Housing		
	% of Total Units	Average Price
Two-Bedroom Units	50%	$842,500
Three-Bedroom Units	25%	$1,001,700
Four-Bedroom Units	25%	$1,348,100
Average Price / SF of Net Saleable Area	100%	$500

D. Affordable Sales Price Calculations

The Affordable Sales Prices calculations are presented in Attachment 2 – Appendix B – Exhibit I. The calculations are based on the following assumptions:

1. The household income information used in the calculations is based on 2020 income statistics for Orange County as a whole. The household incomes for moderate income households are produced and distributed annually by HCD.[12]

2. The Affordable Sales Price estimates are based on the calculation methodology imposed by H&SC Section 50052.5. The calculations include the elements described in the following sections of this report.

Household Size

The household incomes applied in the Affordable Sales Price calculations are set at the number of bedrooms in the home plus one. For example, the imputed household size for a three-bedroom home is four persons. H&SC Section 50052.5 refers to this as "the household size appropriate for the unit." However, this is not meant to be an occupancy cap; it is simply a benchmark used to create a consistent methodology for calculating the Affordable Sales Price.

Household Income

For moderate income households, H&SC Section 50052.5 uses 110% of AMI for a household size equal to the number of bedrooms in the home plus one. This measurement is only used for setting the Affordable Sales Prices. Households with incomes of up to 120% AMI would qualify to reside in moderate income units.

Income Allocated to Housing-Related Expenses

H&SC Section 50052.5 allocates 35% of the benchmark household income to the payment of housing-related expenses.

[12] As of April 23, 2020 HCD had not yet published 2020 income information. For the purposes of this Financial Analysis KMA estimated the moderate income amounts based on an extrapolation from the Orange County median income published by HUD on April 1, 2020. It is possible that the information published by HCD for 2020 may vary somewhat from these estimates.

Housing-Related Expenses

Based on research undertaken by KMA, the variable housing related expense assumptions used in this analysis are presented in the following table:

Variable Housing Related Expenses – Ownership Housing		
	Monthly Utilities Allowances [13]	Monthly HOA, Insurance & Maintenance
Two-Bedroom Units	$171	$500
Three-Bedroom Units	$226	$550
Four-Bedroom Units	$281	$575

The property tax expense estimate is based on 1.08% of the home's estimated Affordable Sales Price. This Affordable Sales Price is applied as the assessed value due to the fact that an irrevocable long-term resale restriction covenant is imposed on the home.

Supportable Mortgage Amount

The mortgage amounts used in the Affordable Sales Price calculations are estimated using the income available after the other housing-related expenses are paid. The Affordable Ownership Housing Regulations state the following:

> *The Maximum Mortgage Amount is equal to the present value of the Income Available for Mortgage Payments over a 30-year term. The discount rate used to determine the present value is set at the Mortgage Interest Rate. The Mortgage Interest Rate will be posted on the City's website, and will be updated monthly.*

[13] The utilities allowances are based on the assumption that the home owners utilities costs are comprised of gas heating, cooking and water heating; basic electric; water; and trash and sewer services. The allowances are based on the Orange County Housing Authority schedule effective October 1, 2019.

In practice, the City has been using the lowest interest rate published during the preceding three month period. As an example, the rate being applied by the City in April 2020 is 2.46%. This rate is significantly lower than the rates for which typical moderate income home buyers will be able to qualify. Common reasons for this are:

1. Credit history and scores that do not fall within the exceptional level required to obtain the lowest interest rate available in the marketplace;

2. Back-end ratios that are often higher than the typical ratios applied in conventional lenders' underwriting standards for the lowest interest rate mortgages;

3. The lowest published interest rate is often a teaser rate that will ultimately adjust to a higher rate that will be unaffordable to the moderate income home buyer; and

4. There is a limited pool of mortgage lenders that are willing to provide loans on homes that are subject to long-term irrevocable resale restrictions. These lenders do not generally offer the lowest interest rates available in the marketplace.

The use of the lowest published interest rate is not required by the Inclusionary Housing Ordinance or by the Affordable Ownership Housing Regulations. The application of this metric generates extremely high Affordable Sales Prices, which can actually only be achieved by home buyers with the ability to make an extraordinarily large down payment.

KMA strongly recommends that the City modify the policy being used to set the mortgage interest rate being applied in the Affordable Sales Price calculations. The mortgage terms used in this pro forma analysis are based on a 50 basis points premium applied to the April 20, 2020 Bankrate site average APR for 30-year fixed interest rate mortgages. This results in a 4.24% interest rate.

Benchmark Down Payment

KMA set the down payment at 10% of the Affordable Sales Price. This represents a benchmark percentage based on the standards set forth in the Affordable Ownership Housing Regulations.

The benchmark down payment is only used for the purpose of setting the Affordable Sales Price. The actual down payment amount can vary from a minimum of 5% to a maximum of 50% of the Affordable Sales Price. However, it is important to understand that the down payment amount does not impact the Affordable Sales Price. Rather, the actual down payment contributed by a home buyer is subtracted from the defined Affordable Sales Price to establish the allowable first trust deed mortgage amount.

Affordable Sales Prices

The Affordable Sales Price estimates for moderate income units are:

Affordable Sales Price Estimates – Ownership Housing	
Two-Bedroom Units	$432,800
Three-Bedroom Units	$475,200
Four-Bedroom Units	$509,700

E. Pro Forma Analyses

KMA prepared two pro forma analysis, which can be described as follows:

1. A pro forma analysis was prepared for a project that includes 40 condominium units. Four of the units are set aside for moderate income households and 36 units are unrestricted market rate units (Existing 10% Production Alternative).

2. A pro forma analysis was prepared for a 40 unit condominium project in which a fee is paid in lieu of producing any affordable units. The analysis is based on the 2019 in-lieu fee schedule, which is currently being applied (Existing In-Lieu Fee Payment Alternative).

The pro forma analyses are organized as follows:

Ownership Housing Pro Forma Analyses	
Table 1:	Estimated Development Costs
Table 2:	Projected Net Sales Revenue
Table 3:	Projected Developer Profit

Existing 10% Production Alternative – Ownership Housing

The pro forma analysis for the Existing 10% Production Alternative is presented in Attachment 2 – Appendix A – Exhibit I. In this alternative 90% of the units are sold at unrestricted market rate prices and 10% of the units are sold to moderate income households at Affordable Sales Prices.

Existing In-Lieu Fee Payment Alternative – Ownership Housing

The pro forma analysis for the Existing In-Lieu Fee Payment Alternative is presented in Attachment 2 – Appendix A – Exhibit II. In this alternative 100% of the units are sold at unrestricted market rate prices, and the in-lieu fee is paid when building permits are issued. A comparison of the pro forma analyses follows:

Pro Forma Comparison – Ownership Housing			
	Existing 10% Production Alternative	Existing In-Lieu Fee Payment Alternative	Difference
Development Costs			
Property Acquisition Costs	$7,623,000	$7,623,000	--0--
Direct Costs	18,392,000	18,392,000	--0--
Indirect Costs	3,940,000	6,406,000	(2,466,000)
Financing Costs	1,733,000	1,938,000	($205,000)
Total Development Costs	$31,688,000	$34,359,000	($2,671,000)

Pro Forma Comparison – Ownership Housing			
	Existing 10% Production Alternative	Existing In-Lieu Fee Payment Alternative	Difference
Net Revenue	$35,658,000	$37,678,000	($2,020,000)
Developer Profit	$3,970,000	$3,319,000	$651,000
As a % of Development Cost	12.5%	9.7%	

As can be seen in the preceding table, under current conditions, the Existing 10% Production Alternative generates a higher developer return than the Existing In-Lieu Fee Payment Alternative. This is attributable to the following factors:

1. The total development costs for the Existing In-Lieu Fee Payment Alternative are $2.67 million higher than the total development costs for the Existing 10% Production Alternative. The differences are largely explained by the following factors:

    a. The scheduled in-lieu fee payment totals $2,349,000. Under the existing Inclusionary Housing Ordinance terms, this payment must be made when building permits are issued.

    b. The additional carrying costs associated with the in-lieu fee payment are estimated at $205,000.

2. The net revenue generated by the Existing In-Lieu Fee Payment Alternative is $2.02 million higher than the net revenue for the Existing 10% Production Alternative.

3. The resulting net profit is $651,000 higher for the Existing 10% Production Alternative than for the Existing In-Lieu Fee Payment Alternative.

Based on the findings of the comparative pro forma analyses it would seem likely that developers would choose to fulfill the Inclusionary Housing requirement on site within the market rate project. However, historically, ownership housing developers have typically requested the right to pay the in-lieu fee. It is likely that this option is selected for the following reasons:

1. The in-lieu fee amount is fixed when building permits are obtained for the project. Developers place a value on certainty.

2. The upside potential for market rate prices can be achieved for 100% of the units in the project.

3. It can be difficult to attract home buyers who meet both the income qualification standards and lenders' underwriting criteria and are willing to purchase a home that is subject to long-term resale restrictions.

F. In-Lieu Fee Analysis: Ownership Housing

In general terms, the financial impact associated with fulfilling Inclusionary Housing requirements within market rate projects is equal to the difference between the achievable market rate sales prices or rents and the Affordable Sales Prices or Affordable Rents for the Inclusionary Housing units. This is known as the "Affordability Gap." The Affordability Gap represents the maximum in-lieu fee that should be charged as part of an Inclusionary Housing program.

KMA prepared Affordability Gap analyses for a condominium/townhome project and a single family home project (Attachment 2 – Appendix B – Exhibit II). These analyses apply the weighted average Affordability Gaps to the bedroom mixes identified in the home sales survey.

As discussed previously, the home sales survey demonstrated significantly higher prices for the single family homes than for condominiums/townhomes. This is partially attributable to the fact that the single family homes are larger than the condominiums/townhomes, and also that a premium is typically paid for detached homes. In the survey, the weighted average sales price per square foot of net saleable area was 38% higher for the single family homes than for the condominiums/townhomes.

As shown in Attachment 2 – Appendix B – Exhibit II, the weighted average Affordability Gaps, and the resulting in-lieu fees, are as follows:

In-Lieu Fees Based on Affordability Gaps – Ownership Housing		
In-Lieu Fee	Condominiums & Townhomes	Single Family Homes
Per Moderate Income Unit	$504,700	$1,635,900
Per Total Unit in the Project	$50,470	$163,590
Per SF of Net Saleable Area	$25.36	$55.34

As can be seen in the preceding table, the in-lieu fee based on the Affordability Gap is estimated at $50,470 per total unit in the condominium and townhome project. Comparatively, the 2019 in-lieu fee under the existing Inclusionary Housing Ordinance is set at $58,736 per total unit in the project. Thus, the currently supportable in-lieu fee for condominium and townhome projects is estimated to be approximately 14% lower than the in-lieu fee applied by the existing 2019 schedule.

It is important to note that the in lieu fee based on the Affordability Gap for single family homes is estimated at $163,590 per total unit in the project. A fee of this magnitude is significantly higher than the in-lieu fee charged in any Southern California city.

V. RENTAL APARTMENT ANALYSIS

The existing Inclusionary Housing Ordinance effectively allows developers to fulfill the affordable housing requirements by allocating 10% of the units in a market rate project to moderate income households. Therefore, KMA applied this requirement as the base case in the analysis. KMA also prepared pro forma analysis for the following alternatives:

1. A 10% low income requirement for a project at the density allowed by zoning; and

2. A Section 65915 density bonus alternative that allocates 11% of the units allowed by the site's zoning to very low income households.

The rental apartment pro forma analyses are used to estimate the financial impacts created by the modifications to the affordability standards that are being tested. The analysis is also used to estimate the supportable in-lieu fees.

A. Supporting Documents: Rental Apartment Analysis

The documents that support the rental apartment analysis are presented in Attachment 3. The pro forma analyses for rental apartment projects are organized as follows:

Financial Analysis – Rental Apartments	
Appendix A	Pro Forma Analyses
Appendix B	Affordability Analyses
Appendix C	Rent Survey

A variety of tools are available to reduce the financial impact associated with the imposition of income and affordability restrictions on rental apartment projects. For example, the Section 65915 density bonus program is commonly used by the developers in jurisdictions that impose Inclusionary Housing requirements. As discussed previously, under the findings of the *Napa* case, a developer must be allowed to fulfill Inclusionary Housing and Section 65915 density bonus requirements with the same affordable units as long as the affordable units meet the more restrictive of the standards imposed by the two programs.

B. Rental Apartment Prototypes

The rental apartment prototypes used in this analysis were created based on the results of the KMA market surveys, and a review of projects that have recently been constructed in

Huntington Beach. The KMA market surveys were also used to estimate the achievable market rate rents for the prototype units. The prototypes used in this analysis reflect the characteristics of recently constructed projects. These prototypes are described in the following table:

Rental Apartment Project Prototypes		
	Moderate & Low Income Alternatives	Very Low Income Density Bonus Alternative
Site Area (Acres)	8.0	8.0
Total Number of Units	400	540
Density (Units Per Acre)	50	67.5
Unit Mix		
Studio Units	60	81
One-Bedroom Units	200	270
Two-Bedroom Units	120	162
Three-Bedroom Units	20	27
Average Unit Sizes (Sq Ft)		
Studio Units	620	620
One-Bedroom Units	820	820
Two-Bedroom Units	1,160	1,160
Three-Bedroom Units	1,550	1,550
Parking		
Total Number of Spaces [14]	750	729
Parking Spaces Per Unit	1.88	1.35
Parking Type	Wrap	Wrap

[14] The citywide and Section 65915 parking standards require 1.0 space for studio and one-bedroom units; and; 2.0 spaces for two-bedroom units. For three-bedroom units the citywide requirement is 2.5 spaces and the Section 65915 standard is 2.0 spaces. The Moderate and Low Income Alternatives include .5 guest spaces per unit. No guest spaces can be required under the Section 65915 standards.

C. Projected Market Rents

In February 2020, KMA surveyed rental apartment projects in Huntington Beach that received four or more stars in the CoStar quality ranking system (Attachment 3 – Appendix C). The purpose of this survey was to derive estimates of the currently achievable market rents for the types of projects likely to be constructed in Huntington Beach. However, the characteristics of actual projects will vary to some degree from the prototypes.

The market rate monthly rent estimates that are used in this pro forma analysis are:

Projected Monthly Market Rate Rents – Rental Apartments	
Average Monthly Rent Per Unit	
Studio Units	$2,652
One-Bedroom Units	$3,189
Two-Bedroom Units	$4,856
Three-Bedroom Units	$5,501
Average Monthly Rent Per SF of Net Leasable Area	$4.01

D. Affordable Rent Calculations

The Inclusionary Housing Ordinance calls for Affordable Rents to be calculated using the methodology imposed by H&SC Section 50053. The calculations are presented in Attachment 3 – Appendix B – Exhibit I, and the assumptions and results can be summarized as follows:

1. The household income information used in the calculations is based on 2020 income statistics for Orange County as a whole. The household incomes are published annually by HUD and are distributed by HCD. [15]

2. The household size appropriate for the unit is based on the H&SC Section 50052.5 standard of the number of bedrooms in the home plus one. As was the case in the Affordable Sales Price calculations, this is a benchmark, not an occupancy cap.

3. The household incomes used in the Affordable Rent calculations are set as follows:[16]

   a. Moderate income at 110% of AMI;

   b. Low income at 60% of AMI; and

   c. Very low income at 50% of AMI.

4. Thirty percent (30%) of defined household income is allocated to housing- expenses.

5. KMA's calculations are based on the assumption that the tenants will be required to pay for gas heating, cooking and water heating; and basic electric services. The October 1, 2019 Orange County Housing Authority utilities allowances were applied to this analysis.

The resulting Affordable Rents are presented in the following table:

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[15] As of April 22, 2020 HCD had not yet published 2020 income information. For the purposes of this Financial Analysis KMA estimated the very low, low and moderate income amounts based on extrapolations from the Orange County median income published by HUD on April 1, 2020. It is possible that the information published by HCD may vary somewhat from these estimates.

[16] The percentages of the AMI used in the Affordable Rent calculations are benchmarks established by H&SC 50053. The incomes limit used to qualify households to occupy moderate income units is based on 120% of AMI as defined in H&SC 50093. The low income limit is defined in H&SC 50079.5 and the very low income limit is defined in H&SC 50105. These limits are meant to reflect 80% and 50% of AMI, respectively. However, HUD adjusts the income levels for Orange County to account for conditions that warrant special consideration. As a result, the current income qualification limits exceed 80% and 50% of AMI.

Affordable Rent Calculations – Rental Apartments			
	Moderate Income	Low Income	Very Low Income
Studio Units			
Maximum Monthly Housing Cost	$1,983	$1,082	$901
(Less) Monthly Utility Allowance	(51)	(51)	(51)
Affordable Rent	$1,932	$1,031	$850
One-Bedroom Units			
Maximum Monthly Housing Cost	$2,266	$1,236	$1,030
(Less) Monthly Utility Allowance	(61)	(61)	(61)
Affordable Rent	$2,205	$1,175	$969
Two-Bedroom Units			
Maximum Monthly Housing Cost	$2,549	$1,391	$1,159
(Less) Monthly Utility Allowance	(80)	(80)	(80)
Affordable Rent	$2,469	$1,311	$1,079
Three-Bedroom Units			
Maximum Monthly Housing Cost	$2,833	$1,545	$1,288
(Less) Monthly Utility Allowance	(103)	(103)	(103)
Affordable Rent	$2,730	$1,442	$1,185

E. Pro Forma Analyses

Moderate Income Alternative – Rental Apartments

The Moderate Income Alternative is based on the existing Inclusionary Housing Ordinance mix of 90% unrestricted market rate units and 10% moderate income units. This provides a baseline against which to measure the impacts associated with imposing stricter affordability requirements than are imposed by the existing Inclusionary Housing Ordinance.

The pro forma analysis is presented in Attachment 3 – Appendix A – Exhibit I, and it is organized as follows:

Moderate Income Alternative Rental Apartments	
Table 1:	Estimated Development Costs
Table 2:	Estimated Stabilized Net Operating Income
Table 3:	Estimated Developer Return

The estimated stabilized developer returns on total investment derived from the Moderate Income Alternative analysis is 6.1%.

Supportable Inclusionary Housing Production Requirements

The pro forma analyses for the Low Income Alternative and the Very Low Income Density Bonus Alternative are presented in Attachment 3 – Appendix A – Exhibits II and III, respectively. The analyses are organized as follows:

Low Income Alternative and Very Low Income Density Bonus Alternative Rental Apartments	
Table 1:	Estimated Development Costs
Table 2:	Estimated Stabilized Net Operating Income
Table 3:	Inclusionary Housing Impact

The pro forma analyses for the Low Income Alternative and the Very Low Income Density Bonus Alternative are presented in Attachment 3 – Appendix A – Exhibit II and Exhibit III, respectively. The results of the analyses are summarized in the following table:

Inclusionary Housing Impacts Analyses Rental Apartments		
	Enhanced / (Reduced) Value	Return on Total Investment
Moderate Income Alternative	N/A	6.1%
Low Income Alternative	($6,300,000)	5.9%
Very Low Income Density Bonus Alternative	$4,505,000	6.2%

The results of the Inclusionary Housing impacts analyses for rental apartments indicate the following:

1. The imposition of a 10% low income Inclusionary Housing requirement is estimated to reduce the prototype rental apartment project's value by $6.3 million. This represents an approximately 14% reduction in the property acquisition costs that can be supported, which is well within the range of impacts typically created by Inclusionary Housing requirements.

2. The Very Low Income Density Bonus Alternative is actually stronger from a financial perspective than the Moderate Income Alternative. If a developer can efficiently make use of the 35% density bonus provided by Section 65915, this alternative clearly presents the most efficient method for fulfilling the City's Inclusionary Housing requirements.

F. In-Lieu Fee Analysis: Rental Apartments

KMA estimated the supportable in-lieu fee amounts for rental apartment projects based on the Affordability Gaps associated with the on-site development of Inclusionary Housing units within market rate rental apartment projects. In-lieu fee analyses were only prepared for the Moderate and Low Income Alternatives. Projects that make use of the Section 65915 density bonus must produce the requisite number of affordable housing units.

The Affordability Gaps for rental apartments are estimated in Attachment 3 - Appendix B – Exhibit II using the following methodology:

1. The analysis is based on the assumption that 10% of the total units in a market rate rental apartment project would be subject to Inclusionary Housing requirements.

2. The differences between the estimated achievable market rate monthly rents and the defined Affordable Rents are calculated for studio, one-bedroom, two-bedroom and three-bedroom units.

3. KMA assumed that the property taxes for projects that include designated affordable housing units would be based on a lower assessed value due to the reduction in net operating income that would be generated by the project. KMA deducted this lower property tax expense from the estimated rent difference.

4. The estimated annual Affordability Gap is equal to the net rent difference minus the property tax savings.

5. The total Affordability Gaps are estimated by capitalizing the annual Affordability Gaps at the threshold returns derived from a pro forma analysis of a market rate development. The results of these calculations are defined as the Net Affordability Gaps.

6. The Net Affordability Gaps are translated into the supportable in-lieu fees per affordable unit and per square foot of net leasable area.

The results of the in-lieu fee analysis are summarized in the following table:

In-Lieu Fees Based on Affordability Gaps – Rental Apartments		
In-Lieu Fee	Moderate Income Alternative	Low Income Alternative
Per Affordable Unit	$192,000	$332,000
Per Total Unit in the Project	$19,200	$33,200
Per SF of Net Leasable Area	$20.70	$35.80

VI. SUMMARY

The following section summarizes the results of this Financial Analysis. The findings provide the basis for KMA's recommendations for updating the Inclusionary Housing Ordinance. A detailed set of policy recommendations are presented in a separate memorandum.

A. Existing Inclusionary Housing Requirements

The Inclusionary Housing requirements that were evaluated in this Financial Analysis can be summarized as follows:

1. The requirements are imposed on all new residential development with three or more units.

2. A 10% affordable housing requirement is imposed on residential development that is subject to the Inclusionary Housing requirements. The existing income restrictions are:

    a. Ownership housing developments are subject to a moderate income unit requirement; and

    b. The base requirement for rental apartment projects is for low income units. However, at the City's discretion affordable units that are built on site within a market rate projects can fulfill the requirement with moderate income units.

B. Residential Development Prototypes

The development scopes for the residential development prototypes that were evaluated in this Financial Analysis are presented in the following table:

Residential Development Prototypes: Development Scopes			
	Ownership Housing	Rental Apartments	
	Condominium Alternative	Moderate & Low Income Alternatives	Very Low Income Density Bonus Alternative
Site Area (Acres)	1.0	8.0	8.0
Total Number of Units	40	400	540
Density (Units Per Acre)	40	50	67.5
<u>Unit Mix</u>			
Studio Units		60	81
One-Bedroom Units		200	270
Two-Bedroom Units	20	120	162
Three-Bedroom Units	20	20	27
Four-Bedroom Units	10		
<u>Average Unit Sizes (Sq Ft)</u>			
Studio Units		620	620
One-Bedroom Units	1,530	820	820
Two-Bedroom Units	1,900	1,160	1,160
Three-Bedroom Units	3,000	1,550	1,550
<u>Parking</u>			
Total Number of Spaces	110	750	729
Parking Spaces Per Unit	2.75	1.88	1.35
Parking Type	Subterranean	Wrap	Wrap

The ownership housing sales price and rental apartment rent estimates applied in this analysis are provided in the following table:

Residential Development Prototypes: Sales Prices and Rents		
	Ownership Housing	Rental Apartments
Unit Mix		
Studio Units		$2,652
One-Bedroom Units		$3,189
Two-Bedroom Units	$837,000	$4,856
Three-Bedroom Units	$991,300	$5.501
Four-Bedroom Units	$1,321,000	
Sales Price/Rent Per Square Foot	$501	$4.01

C. Conclusions

Based on the results of the preceding Financial Analysis, KMA reached the following conclusions:

1. Inclusionary Housing Requirements:

   a. The 10% moderate income requirement for ownership housing development continues to be supportable.

   b. The 10% low income requirement for rental apartment projects is supportable. There is no need to provide an option for moderate income units to be used as a substitute when the units are provided on site within a market rate project.

2. The maximum in-lieu fee amounts are currently estimated as follows:

Supportable In-Lieu Fees		
	Ownership Housing	Rental Apartments [17]
In-Lieu Fee Amounts		
Per Affordable Unit	$504,700	$332,000
Per Total Unit	$50,470	$33,200
Per Square Foot of Saleable/Leasable Area	$25.36	$35.80

[17] Based on a 10% low income unit Inclusionary Housing Requirement.

ATTACHMENT 1

INCLUSIONARY HOUSING PROGRAM SURVEY
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

ATTACHMENT 1

INCLUSIONARY HOUSING PROGRAM SURVEY
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

				Rental Development			Ownership Developent		
Jurisdiction	Compliance Options	Set Aside %	On-site % Varies	Threshold Project Size	% of AMI	Covnenant Period	Threshold Project Size	% of AMI	Covnenant Period
I. Inclusionary Requirements: Both Rental and Ownership Projects									
Albany	Create on-site units; create off-site units; preserve or rehab existing housing; pay in-lieu fee; donate land	15%	Yes	5		Perpetual	5		Perpetual
Avalon	Create on-site units; create off-site units; pay in-lieu fee	20%	No	4		55	4		55
Brea	Create on-site units; create off-site units; preserve or rehab existing housing; pay in-lieu fee; donate land	10%	No			55		120%	10
Campbell	Create on-site units; create off-site units; preserve or rehab existing housing; pay in-lieu fee; donate land	15%	No			55		120%	45
Capitola	Create on-site units; pay in-lieu fee	15%	Yes				7	120%	Life of Bldg
Chula Vista	Create on-site units; create off-site units; preserve or rehab existing housing; pay in-lieu fee; donate land	10%	No	50	80% /120%	Life of Bldg	50	80% /120%	Life of Bldg
Colma	Create on-site units; pay in-lieu fee	20%	No	5		55	5		45
Concord	Create on-site units; create off-site units; preserve or rehab existing housing; pay in-lieu fee	10%	Yes	5		55	5		45
Contra Costa County [1]	Create on-site units; create off-site units; pay in-lieu fee; donate land	15%	No	5			5		3
Cupertino	1-7 units pays in-lieu fee. Create on-site units; create off-site units; pay impact/linkage fee; donate land	15%	No	7	50% /80%	99	7	50% /120%	99
Davis	Create on-site units; preserve or rehab existing housing; pay in-lieu fee; donate land	5% to 25%	No	5	80%	Perpetual	5	120%	Perpetual
Dublin	Create on-site units; create off-site units; pay in-lieu fee; donate land	12.5%	No	20		55	20		55
Emeryville	Create on-site units; pay impact/linkage fee	12%/20%	No			55	10		55
Fort Bragg	Create on-site units	10% to 20%		5	80% /120%		5	100% /120%	15
Hayward	Create on-site units; create off-site units; pay in-lieu fee; pay impact/linkage fee; donate land	15%	No	20	80%	55	20	120%	45
Huntington Beach	Create on-site units; create off-site units; preserve or rehab existing housing; pay in-lieu fee	10%	No	3	80%	55	3	120%	45
Irvine	Create on-site units; create off-site units; preserve or rehab existing housing; pay in-lieu fee; donate land	15%	No	50		30	50		30
Los Altos [1]	Create on-site units; create off-site units	10%	No	10		30	10		30

ATTACHMENT 1

INCLUSIONARY HOUSING PROGRAM SURVEY
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

				Rental Development			Ownership Developent		
Jurisdiction	Compliance Options	Set Aside %	On-site % Varies	Threshold Project Size	% of AMI	Covnenant Period	Threshold Project Size	% of AMI	Covnenant Period
Menlo Park	Create on-site units; create off-site units; pay in-lieu fee	10%	Yes	5	80% /120%		5	80% /120%	
Mill Valley	Create on-site units	25%	Yes	4	120%	Perpetual	4	120%	Perpetual
Nevada County [1]	Create on-site units; create off-site units		No	20		30	20		30
Oxnard	Create on-site units; pay in-lieu fee	10%	No	10		55	10		
Pacifica	Create on-site units; create off-site units; pay in-lieu fee; donate land	15%	No	8		55	8		45
Palo Alto	Create on-site units; create off-site units; preserve or rehab existing housing; pay in-lieu fee	15%	Yes			59			59
Pasadena	Create on-site units; create off-site units; preserve or rehab existing housing; pay in-lieu fee; donate land	15%	No	10			10	120%	45
Petaluma	Create on-site units; pay in-lieu fee; donate land	15%	No			30			30
Pleasanton	Create on-site units; create off-site units; pay in-lieu fee; donate land; credit transfers; other alternate methods of compliance	15%	Yes	15			15		Perpetual
Redwood City	Create on-site units; create off-site units; preserve or rehab units; pay impact/linkage fee; donate land		No	5		30	5		30
San Bruno	Create on-site units; create off-site units; preserve or rehab existing housing; pay in-lieu fee; donate land	15%	No	10		55	10		45
San Diego	Create on-site units; create off-site units; pay in-lieu fee; donate land	10% to 15%	No	10	50% or 80%	55		100% or 120%	
San Jose	Create on-site units; create off-site units; preserve or rehab units; in-lieu fee; donate land; credit transfers	15%	No	20	50%/ 80%	Perpetual	20	120%	Perpetual
San Juan Capistrano	Create on-site units; create off-site units; preserve or rehab	10%	No	2		55	2		55
San Mateo County	Create on-site units	10%	Yes	11	80%	Life of Bldg	11	120%	45
San Rafael	Create on-site units; pay in-lieu fee	10%	No	2			2	120%	
Santa Cruz	Create on-site units; create off-site units; pay in-lieu fee; donate land	15%	Yes	2	80%	Perpetual	2	120%	Perpetual
Santa Monica	Create on-site units; create off-site units; pay in-lieu fee; donate land	5% to 30%	Yes	2		55	2		55
Sonoma	Create on-site units	25%	Yes	5	120%	55	5	120%	55

INCLUSIONARY HOUSING PROGRAM SURVEY
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

				Rental Development			Ownership Developent		
Jurisdiction	Compliance Options	Set Aside %	On-site % Varies	Threshold Project Size	% of AMI	Covnenant Period	Threshold Project Size	% of AMI	Covnenant Period
Sonoma County	Create on-site units; create off-site units; pay in-lieu fee; donate land	20%	Yes		60%	55		80%	30
South San Francisco	Create on-site units; create off-site units; preserve or rehab existing housing; pay in-lieu fee	20%	No	4		55	4		55
Sunnyvale	Create on-site units; create off-site units; preserve or rehab existing housing; pay in-lieu fee	12.5%	No	4	80%	55		120%	30
Tiburon	Create on-site units; create off-site units; pay in-lieu fee	15%		3		Perpetual	3		Perpetual
Union City	Create on-site units; create off-site units; pay in-lieu fee	15%	No	7			7		
West Sacramento	Create on-site units; create off-site units; preserve or rehab existing housing; pay in-lieu fee; donate land	10%	Yes			55		80%	45
West Hollywood	Create on-site units; create off-site units			2			2		
II. <u>Inclusionary Requirements: Ownership Projects Only</u>									
Alameda	Create on-site units; create off-site units; pay in-lieu fee	5%	No				5		59
Danville	Create on-site units; pay in-lieu fee	10%	Yes				7	110%	20
Fremont	Create on-site units; create off-site units; preserve or rehab existing housing; pay in-lieu fee; donate land	15%	Yes					110%	30
Lafayette [2]	Create on-site units; create off-site units	15%	No				2		45
Monterey	Create on-site units; donate land	20%	No				6		Perpetual
Mountain View	Create on-site units; pay in-lieu fee	10%	No				3	100%	55
Rohnert Park	Create on-site units; create off-site units; pay in-lieu fee	15%	No				5		55
San Leandro	Create on-site units; pay in-lieu fee	15%	Yes						55
San Mateo County	Create on-site units; create off-site units; pay in-lieu fee; donate land	20%	No				5		55
Santa Barbara	Create on-site units; pay in-lieu fee; donate land	15%	No				2	160%	90

ATTACHMENT 1

INCLUSIONARY HOUSING PROGRAM SURVEY
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

				Rental Development			Ownership Developent		
Jurisdiction	Compliance Options	Set Aside %	On-site % Varies	Threshold Project Size	% of AMI	Covnenant Period	Threshold Project Size	% of AMI	Covnenant Period
III. Inclusionary for Ownership Projects & Impact Fee for Rental Projects									
Berkeley	Create on-site units; pay in-lieu fee	20%	No				5	80%	Perpetual
San Carlos	Create on-site units; create off-site units; pay impact/linkage fee	15%	Yes			55	2		45
Truckee [2]	Create on-site units; create off-site units; preserve or rehab existing housing; pay in-lieu fee; pay impact/linkage fee; donate land	15%	No	7		Perpetual	7		Perpetual
IV. Mandatory Inclusionary for Ownership Projects & Voluntary Inclusionary for Rental Projects									
Pittsburg	Create on-site units; pay in-lieu fee	15%	Yes				5		
Salinas	Create on-site units; create off-site units; donate land	20%	No				10		30
San Juan Bautista	Create on-site units; pay impact/linkage fee	6%							
San Luis Obispo	Create on-site units; pay in-lieu fee; donate land	3%	Yes			55	5		45
San Marcos	Create on-site units; create off-site units; preserve or rehab existing housing; pay in-lieu fee; donate land	15%	No			55		120%	55
Solana Beach	Create on-site units; create off-site units; preserve or rehab existing housing; pay impact/linkage fee	15%	No	5		55	5		45
V. Rental Projects Only									
Glendale	Create on-site units; create off-site units; pay in-lieu fee; donate land	15%	No	8	80%	55			

[1] The program requirements are only applied in designated areas of the jurisdiction.
[2] The program requirements are applied in the entire jurisdiction, but the requirements vary by zones, neighborhood, or districts.

ATTACHMENT 2

OWNERSHIP HOUSING DEVELOPMENT
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

APPENDIX A

CONDOMINIUM PROTOTYPE
OWNERSHIP HOUSING DEVELOPMENT
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

APPENDIX A - EXHIBIT I

CONDOMINIUM PROTOTYPE
OWNERSHIP HOUSING DEVELOPMENT
PRO FORMA ANALYSES
EXISTING 10% PRODUCTION ALTERNATIVE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

APPENDIX A - EXHIBIT I - TABLE 1

ESTIMATED DEVELOPMENT COSTS
CONDOMINIUM PROTOTYPE: OWNERSHIP HOUSING DEVELOPMENT
PRO FORMA ANALYSES
EXISTING 10% PRODUCTION ALTERNATIVE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

I.	**Property Acquisition Costs**	[1]	43,560	Sf of Land	$175	/Sf of Land		$7,623,000
II.	**Direct Costs**	[2]						
	On-Site Improvements/Landscaping		43,560	Sf of Land	$20	/Sf of Land	$871,000	
	1st Level Subterranean Parking Spaces	[3]	110	Spaces	$25,000	/Space	2,750,000	
	Building Costs	[4]	93,647	Sf of GBA	$125	/Sf of GBA	11,706,000	
	Contractor/DC Contingency Allow		20%	Other Direct Costs			3,065,000	
	Total Direct Costs							$18,392,000
III.	**Indirect Costs**							
	Architecture, Engineering & Consulting		6.0%	Direct Costs			$1,104,000	
	Public Permits & Fees	[5]	40	Units	$20,000	/Unit	800,000	
	Taxes, Insurance, Legal & Accounting		3.0%	Direct Costs			552,000	
	Marketing		40	Units	$2,500	/Unit	100,000	
	Developer Fee	[6]	40	Units	$29,900	/Unit	1,196,000	
	Soft Cost Contingency Allowance		5.0%	Other Indirect Costs			188,000	
	Total Indirect Costs							$3,940,000
IV.	**Financing Costs**							
	Interest During Construction	[7]					$1,284,000	
	Loan Origination Fees		60.0%	Loan to Cost	2.5	Points	449,000	
	Total Financing Costs							$1,733,000
V.	**Total Construction Cost**		40	Units	$602,000	/Unit		$24,065,000
	Total Development Cost		40	Units	$792,000	/Unit		$31,688,000

1 Estimated based on a survey of the sales of residentially zoned land in Huntington Beach between June 2016 and August 2019.
2 Based on the estimated costs for similar uses.
3 Based on 2.0 spaces for Two-Bedroom Units; 2.5 spaces for Three-Bedroom Units; 2.5 spaces for Four-Bedroom Units; and 0.50 spaces per unit for guest parking.
4 Includes contractors' fees, general requirements, builder's risk insurance and a direct cost contingency allowance.
5 Based on estimates prepared for other projects within Huntington Beach.
6 Based on the Developer Fee per unit that would be anticipated for a project in which 100% of the units are sold at unrestricted market rate prices.
7 Assumes a 6.0% interest cost for debt; an 18 month construction period; a 5 month absorption period; 30% of the units are presold and close during first month after completion; and 2.5 points for loan origination fees.

APPENDIX A - EXHIBIT I - TABLE 2

PROJECTED NET SALES REVENUE
CONDOMINIUM PROTOTYPE: OWNERSHIP HOUSING DEVELOPMENT
PRO FORMA ANALYSES
EXISTING 10% PRODUCTION ALTERNATIVE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

I.	**Gross Sales Revenue**						
	Market Rate Units [1]						
	Two-Bedroom Units	18	Units @	$837,000	/Unit	$15,066,000	
	Three-Bedroom Units	9	Units @	$991,300	/Unit	8,922,000	
	Four-Bedroom Units	9	Units @	$1,321,700	/Unit	$11,895,000	
	Moderate Income Units [2]						
	Two-Bedroom Units	2	Units @	$432,800	/Unit	866,000	
	Three-Bedroom Units	1	Unit @	$475,200	/Unit	475,000	
	Four-Bedroom Units	1	Unit @	$509,700	/Unit	510,000	
	Total Gross Sales Revenue						$37,734,000
II.	**Cost of Sales**						
	Commissions	3.0%	Gross Sales Revenue			$1,132,000	
	Closing Costs	2.0%	Gross Sales Revenue			755,000	
	Home Buyer Warranties	0.5%	Gross Sales Revenue			189,000	
	Total Cost of Sales						($2,076,000)
III.	**Net Revenue**						$35,658,000

[1] Based on a sales survey undertaken by KMA in February 2020 (See APPENDIX C). For the two- and three-bedroom units a 15% premium is added for new construction. The four-bedroom units in the survey were constructed recently, so no premium was applied. The weighted average sales price equates to $501 per square foot of saleable area.

[2] See APPENDIX B - EXHIBIT I. Equal to the lesser of the calculated affordable sales price or a 30% discount from the projected market price.

APPENDIX A - EXHIBIT I - TABLE 3

PROJECTED DEVELOPER PROFIT
CONDOMINIUM PROTOTYPE: OWNERSHIP HOUSING DEVELOPMENT
PRO FORMA ANALYSES
EXISTING 10% PRODUCTION ALTERNATIVE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

I.	**Net Revenue**		$35,658,000	
II.	**Total Development Cost**	See APPENDIX A - EXHIBIT I - TABLE 1	$31,688,000	
III.	**Developer Profit**	12.5% Total Development Cost		$3,970,000

APPENDIX A - EXHIBIT II

CONDOMINIUM PROTOTYPE
OWNERSHIP HOUSING DEVELOPMENT
PRO FORMA ANALYSES
EXISTING IN-LIEU FEE PAYMENT ALTERNATIVE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

APPENDIX A - EXHIBIT II - TABLE 1

ESTIMATED DEVELOPMENT COSTS
CONDOMINIUM PROTOTYPE: OWNERSHIP HOUSING DEVELOPMENT
PRO FORMA ANALYSES
EXISTING IN-LIEU FEE PAYMENT ALTERNATIVE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

I.	**Property Acquisition Costs**	1	43,560	Sf of Land	$175	/Sf of Land		$7,623,000
II.	**Direct Costs**	2						
	On-Site Improvements/Landscaping		43,560	Sf of Land	$20	/Sf of Land	$871,000	
	1st Level Subterranean Parking Spaces	3	110	Spaces	$25,000	/Space	2,750,000	
	Building Costs		93,647	Sf of GBA	$125	/Sf of GBA	11,706,000	
	Contractor/DC Contingency Allow	4	20%	Other Direct Costs			3,065,000	
	Total Direct Costs							$18,392,000
III.	**Indirect Costs**							
	Architecture, Engineering & Consulting		6.0%	Direct Costs			$1,104,000	
	Public Permits & Fees	5	40	Units	$20,000	/Unit	800,000	
	In-Lieu Fee	6	40	Units	$58,736	/Unit	2,349,000	
	Taxes, Insurance, Legal & Accounting		3.0%	Direct Costs			552,000	
	Marketing		40	Units	$2,500	/Unit	100,000	
	Developer Fee		3.0%	Gross Sales Revenue			1,196,000	
	Soft Cost Contingency Allowance		5.0%	Other Indirect Costs			305,000	
	Total Indirect Costs							$6,406,000
IV.	**Financing Costs**							
	Interest During Construction	7					$1,452,000	
	Loan Origination Fees		60.0%	Loan to Cost	2.5	Points	486,000	
	Total Financing Costs							$1,938,000
V.	**Total Construction Cost**		40	Units	$668,000	/Unit		$26,736,000
	Total Development Cost		40	Units	$859,000	/Unit		$34,359,000

1 Estimated based on a survey of the sales of residentially zoned land in Huntington Beach between June 2016 and August 2019.
2 Based on the estimated costs for similar uses.
3 Based on 2.0 spaces for Two-Bedroom Units; 2.5 spaces for Three-Bedroom Units; 2.5 spaces for Four-Bedroom Units; and 0.50 spaces per unit for guest parking.
4 Based on the profit as a percentage of Total Development Cost estimated to be generated by the
5 Based on estimates prepared for other projects within Huntington Beach.
6 Based on the 2019 In-Lieu Fee for a 40 unit project.
7 Assumes a 6.0% interest cost for debt; an 18 month construction period; a 5 month absorption period; 30% of the units are presold and close during first month after completion; and 2.5 points for loan origination fees.

APPENDIX A - EXHIBIT II - TABLE 2

PROJECTED NET SALES REVENUE
CONDOMINIUM PROTOTYPE: OWNERSHIP HOUSING DEVELOPMENT
PRO FORMA ANALYSES
EXISTING IN-LIEU FEE PAYMENT ALTERNATIVE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

I.	**Gross Sales Revenue** [1]						
	Two-Bedroom Units	20	Units @	$837,000	/Unit	$16,740,000	
	Three-Bedroom Units	10	Units @	$991,300	/Unit	$9,913,000	
	Four-Bedroom Units	10	Units @	$1,321,700	/Unit	$13,217,000	
	Total Gross Sales Revenue						$39,870,000
II.	**Cost of Sales**						
	Commissions	3.0%	Gross Sales Revenue			$1,196,000	
	Closing Costs	2.0%	Gross Sales Revenue			797,000	
	Home Buyer Warranties	0.5%	Gross Sales Revenue			199,000	
	Total Cost of Sales						($2,192,000)
III.	**Net Revenue**						$37,678,000

[1] Based on a sales survey undertaken by KMA in February 2020 (See APPENDIX C). For the two- and three-bedroom units a 15% premium is added for new construction. The four-bedroom units in the survey were constructed recently, so no premium was applied. The weighted average sales price equates to $501 per square foot of saleable area.

APPENDIX A - EXHIBIT II - TABLE 3

PROJECTED DEVELOPER PROFIT
CONDOMINIUM PROTOTYPE: OWNERSHIP HOUSING DEVELOPMENT
PRO FORMA ANALYSES
EXISTING IN-LIEU FEE PAYMENT ALTERNATIVE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

I.	**Net Revenue**	See APPENDIX A - EXHIBIT II - TABLE 2	$37,678,000
II.	**Total Development Cost**	See APPENDIX A - EXHIBIT II - TABLE 1	$34,359,000
III.	**Developer Profit**	9.7% Total Development Cost	$3,319,000

APPENDIX B

OWNERSHIP HOUSING DEVELOPMENT
AFFORDABILITY ANALYSES
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

APPENDIX B - EXHIBIT I

AFFORDABLE SALES PRICE CALCULATIONS [1]
MODERATE INCOME HOUSEHOLDS
2020 INCOME STANDARDS
OWNERSHIP HOUSING DEVELOPMENT
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

			Two-Bedroom Units	Three-Bedroom Units	Four-Bedroom Units
I.	**Income Information**				
	Area Median Income	1	$92,700	$103,000	$111,250
	Household Income @ 110% Median	2	$101,970	$113,300	$122,380
	Income Allotted to Housing @ 35% of Income		$35,690	$39,660	$42,830
II.	**Expenses**				
	Annual Utilities Allowance	3	$2,052	$2,712	$3,372
	HOA, Maintenance & Insurance		6,000	6,600	6,900
	Property Taxes @ 1.08% of Affordable Sales Price	4	4,670	5,130	5,510
	Total Expenses		$12,722	$14,442	$15,782
III.	**Income Available for Mortgage**		$22,968	$25,218	$27,048
IV.	**Affordable Sales Price**				
	Supportable Mtg @ 4.24% Interest	5	$389,500	$427,700	$458,700
	Home Buyer Down Payment @ 10% Aff Sales Price	4	43,300	47,500	51,000
	Affordable Sales Price		$432,800	$475,200	$509,700

[1] Based on the 2020 Orange County median incomes published by the California Housing & Community Development Department (HCD). The benchmark household size is set at the number of bedrooms in the unit plus one.
[2] Based on the California Health & Safety Code Section 50052.5 calculation methodology.
[3] Based on the Orange County Housing Authority utility allowances effective as of 10/1/19. Assumes: Gas Cooking, Gas Heating, and Gas Water Heater; Basic Electric; Water, Trash/Sewer.
[4] Based on the August 15, 2011 Inclusionary Housing Regulations.
[5] Based on a 50 basis points premium applied to the April 20, 2020 Bankrate site average for 30-year fixed interest rate mortgages.

Prepared by: Keyser Marston Associates
File name: HB Own Inclusionary 5 6 20; ASP

APPENDIX B - EXHIBIT II

IN-LIEU FEE ANALYSIS
AFFORDABILITY GAP APPROACH - MODERATE INCOME
OWNERSHIP HOUSING DEVELOPMENT
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

			Condominium & Townhome Units	Single Family Homes
I.	**Sales Price Difference**			
A.	**Two-Bedroom Units**			
	Market Rate Units		$837,000	
	Affordable Sales Price	1	432,800	
	Difference		$404,200	
B.	**Three-Bedroom Units**			
	Market Rate Units		$991,300	$2,371,400
	Affordable Sales Price	1	475,200	475,200
	Difference		$516,100	$1,896,200
C.	**Four-Bedroom Units**			
	Market Rate Units		$1,321,700	$1,949,100
	Affordable Sales Price	1	509,700	509,700
	Difference		$812,000	$1,439,400
II.	**Distribution of Affordable Units**			
	Two-Bedroom Units		2	
	Three-Bedroom Units		1	48%
	Four-Bedroom Units		1	52%
III.	**Net Affordability Gap Per Moderate Income Unit**			
	Affordability Gap Per Moderate Income Unit		$534,100	$1,658,700
	(Less) Reduced Cost of Sales Per Affordable Unit	2	(29,400)	(22,800)
	Net Affordability Gap Per Moderate Income Unit		$504,700	$1,635,900
IV.	**In-Lieu Fee**			
	Per Total Unit		$50,470	$163,590
	Per Square Foot of Net Saleable Area		$25.36	$55.34

[1] See APPENDIX B - EXHIBIT I.
[2] The Cost of Sales consist of: Commissions @ 3.0%; Closing Costs @ 2.0%; and Home Buyer Warranties @ 0.50%.

APPENDIX C

OWNERSHIP HOUSING DEVELOPMENT
HOME SALES SURVEY
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

APPENDIX C

HOME SALES SURVEY
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

	Address	Zip Code	Unit Size (SF)	Sales Price Total	Sales Price Per SF	Year Built
I.	**Condominium & Townhome Units**					
	Two-Bedroom Units					
	21383 Kennedy Ln	92646	1,472	$379,949	$258	2012
	17552 Van Buren Ln	92647	1,271	$538,500	$424	1995
	20171 Sealpoint Ln #206	92646	1,421	$570,000	$401	1999
	20191 Sealpoint Ln #202	92646	1,332	$575,000	$432	1999
	20171 Sealpoint Ln #105	92646	1,246	$580,000	$465	1999
	415 Townsquare Ln #302	92648	1,038	$580,000	$559	1990
	20171 Sealpoint Ln #107	92646	1,174	$594,000	$506	1998
	8312 Atlanta Avenue #102	92646	1,316	$600,000	$456	1991
	8306 Atlanta Ave #102	92646	1,242	$610,000	$491	1991
	415 Townsquare Ln #103	92648	1,038	$635,000	$612	1990
	1516 Pacific Coast #101	92648	1,300	$685,000	$527	1992
	18858 Milos Cir	92648	1,794	$695,000	$387	1993
	4392 Lahaina Dr #30	92649	1,400	$711,000	$508	2019
	376 5th St	92648	1,810	$875,000	$483	1999
	21386 Armilla Cir	92648	1,843	$940,000	$510	2005
	7976 Aldea Cir	92648	1,843	$950,000	$515	2005
	21339 Cieza Cir	92648	1,843	$950,000	$515	2005
	21387 Armilla Cir	92648	1,843	$960,000	$521	2004
	19335 Brooktrail Ln	92648	2,245	$950,000	$423	1991
	21387 Armilla Cir	92648	1,843	$960,000	$521	2004
	7967 Osuna Cir	92648	1,877	$975,000	$519	2005
	Minimum		1,038	$379,949	$258	1990
	Maximum		2,245	$975,000	$612	2019
	Average		1,533	$729,200	$476	1999
	Three-Bedroom Units					
	7545 Shady Glen Cir	92648	1,407	$464,648	$330	1998
	18775 Chapel Ln	92646	1,773	$678,000	$382	1991
	16432 Poipu Ln	92649	1,512	$707,000	$468	2014
	7675 Timber Cir #2	92648	1,846	$745,000	$404	2003
	8158 Constantine Dr	92646	2,132	$745,000	$349	1997
	6227 Pacific Pointe Dr #30	92648	1,993	$850,000	$426	2002
	8243 Noelle Dr	92646	2,035	$980,000	$482	2013
	21445 Hayley Ln	92646	1,926	$1,010,000	$524	2013
	19331 Brooktrail Ln	92648	2,027	$1,025,000	$506	1991
	19262 Surfwave Dr	92648	2,430	$1,085,000	$447	1997
	16377 26th St #102	90742	1,837	$1,200,000	$653	2016
	Minimum		1,407	$464,648	$330	1991
	Maximum		2,430	$1,200,000	$653	2016
	Average		1,902	$862,700	$454	2003

Source: Redfin. The survey includes executed sales that occurred between March 2019 and March 2020.
Prepared by: Keyser Marston Associates, Inc.
File name: HB Own Inclusionary 5 6 20; Sales Survey

APPENDIX C

HOME SALES SURVEY
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

Address	Zip Code	Unit Size (SF)	Sales Price Total	Sales Price Per SF	Year Built
Four-Bedroom Units					
21396 Abigail Ln	92646	2,431	$1,094,000	$450	2013
8255 Kendall Dr	92646	2,431	$1,099,000	$452	2013
8373 Sage Dr	92646	2,431	$1,108,000	$456	2010
8389 Noelle Dr	92646	2,606	$1,150,000	$441	2013
8237 Kendall Dr	92646	2,778	$1,170,000	$421	2013
8200 Noelle Dr	92646	3,604	$1,375,000	$382	2013
8318 Noelle Dr	92646	3,604	$1,375,000	$382	2012
8220 Noelle Dr	92646	3,604	$1,415,000	$393	2013
21254 Baeza Cir	92648	3,055	$1,534,500	$502	2004
21307 Andalucia Ln	92648	3,459	$1,897,000	$548	2004
Minimum		2,431	$1,094,000	$382	2004
Maximum		3,604	$1,897,000	$548	2013
Average		3,000	$1,321,800	$441	2011

II. **Single Family Homes** [2]

Address	Zip Code	Unit Size (SF)	Sales Price Total	Sales Price Per SF	Year Built
Three-Bedroom Units					
4861 Coveview Dr	92649	2,000	$1,212,500	$606	2011
627 Frankfort Ave	92648	3,407	$1,565,000	$459	2012
1009 California St	92648	3,333	$1,650,000	$495	2019
610 17th St	92648	2,952	$1,740,000	$589	2014
624 14th St	92648	2,875	$1,900,000	$661	2018
622 14th St	92648	2,875	$1,950,000	$678	2018
615 13th St	92648	2,900	$2,075,000	$716	2019
512 8th St	92648	2,875	$2,090,000	$727	2019
613 13th St	92648	2,900	$2,095,000	$722	2019
1004 Huntington St	92648	3,285	$2,100,000	$639	2018
623 13th St	92648	2,900	$2,149,900	$741	2020
314 3rd St	92648	2,875	$2,150,000	$748	2018
514 11th St	92648	2,853	$2,150,000	$754	2016
414 9th St	92648	2,900	$2,225,000	$767	2019
412 9th St	92648	2,875	$2,225,000	$774	2019
312 3rd St	92648	2,850	$2,250,000	$789	2019
310 3rd St	92648	2,850	$2,270,000	$796	2019
809 Huntington St	92648	3,350	$2,295,000	$685	2018
314 3rd St	92648	2,850	$2,425,000	$851	2019
124 7th	92648	2,875	$2,725,000	$948	2020
Minimum		2,000	$1,212,500	$459	2011
Maximum		3,407	$2,725,000	$948	2020
Average		2,929	$2,062,100	$704	2018

Source: Redfin. The survey includes executed sales that occurred between March 2019 and March 2020.
Prepared by: Keyser Marston Associates, Inc.
File name: HB Own Inclusionary 5 6 20; Sales Survey

APPENDIX C

HOME SALES SURVEY
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

			Sales Price		
Address	Zip Code	Unit Size (SF)	Total	Per SF	Year Built
Four-Bedroom Units					
17315 Wareham Ln	92649	1,995	$1,170,000	$586	2010
17301 Wareham Ln	92649	2,200	$1,175,000	$534	2010
10242 Thompson Dr	92646	2,926	$1,212,000	$414	2015
17321 Wareham Ln	92649	2,089	$1,249,900	$598	2010
10241 Patch Dr	92646	2,693	$1,290,000	$479	2015
10192 Thompson Dr	92646	2,926	$1,335,000	$456	2015
19741 Wardlow Ln	92646	3,435	$1,450,000	$422	2015
505 16th St	92648	2,875	$1,500,000	$522	2010
9211 Sheridan Dr	92646	3,253	$1,514,900	$466	2015
17322 Osterville Ln	92649	2,758	$1,530,000	$555	2013
627 Frankfort Ave	92648	3,407	$1,565,000	$459	2012
624 13th St	92648	2,910	$1,645,000	$565	2015
1009 California St	92648	3,333	$1,650,000	$495	2019
609 17th St	92648	2,870	$1,700,000	$592	2019
611 17th St	92648	2,870	$1,750,000	$610	2019
17472 Oakbluffs Ln	92649	3,569	$1,888,000	$529	2015
4862 Orleans Dr	92649	3,555	$1,998,000	$562	2016
510 8th St	92648	2,875	$1,999,999	$696	2018
4891 Orleans Dr	92649	3,628	$2,050,000	$565	2015
1019 California St	92648	3,374	$2,160,000	$640	2018
1737 Park St	92648	3,176	$2,554,000	$804	2018
121 7th St	92648	2,877	$2,900,000	$1,008	2015
Minimum		1,995	$1,170,000	$414	2010
Maximum		3,628	$2,900,000	$1,008	2019
Average		2,982	$1,694,900	$568	2015

1 Due to lack of sales, the condominium/townhomes sales survey is limited to homes built after 1990.
2 The of single family home sales survey is limited to homes built after 2010.

Source: Redfin. The survey includes executed sales that occurred between March 2019 and March 2020.
Prepared by: Keyser Marston Associates, Inc.
File name: HB Own Inclusionary 5 6 20; Sales Survey

ATTACHMENT 3

RENTAL APARTMENT DEVELOPMENT
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

APPENDIX A

RENTAL APARTMENT DEVELOPMENT
PRO FORMA ANALYSES
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

APPENDIX A - EXHIBIT I

RENTAL APARTMENT DEVELOPMENT
PRO FORMA ANALYSES
10% INCLUSIONARY UNITS - MODERATE INCOME ALTERNATIVE
DENSITY @ 50 UNITS PER ACRE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

APPENDIX A - EXHIBIT I - TABLE 1

ESTIMATED DEVELOPMENT COSTS
RENTAL APARTMENT DEVELOPMENT
10% INCLUSIONARY UNITS - MODERATE INCOME ALTERNATIVE
DENSITY @ 50 UNITS PER ACRE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

I.	**Property Acquisition Costs**	[1]	348,480	Sf of Land	$150	/Sf of Land		$52,272,000
II.	**Direct Costs**	[2]						
	On-Site Improvements/Landscaping		348,480	Sf of Land	$20	/Sf of Land	$6,970,000	
	Above-Ground Parking Spaces	[3]	750	Spaces	$25,000	/Space	18,750,000	
	Building Costs		464,250	Sf of GBA	$125	/Sf of GBA	58,031,000	
	Contractor/DC Contingency Allow		20%	Other Direct Costs			16,750,000	
	Total Direct Costs		464,250	Sf of GBA	$216	/Sf of GBA		$100,501,000
III.	**Indirect Costs**							
	Architecture, Engineering & Consulting		8%	Direct Costs			$8,040,000	
	Public Permits & Fees	[4]	400	Units	$20,000	/Unit	8,002,000	
	Taxes, Insurance, Legal & Accounting		3%	Direct Costs			3,015,000	
	Marketing		400	Units	$5,000	/Unit	2,001,000	
	Developer Fee		5%	Direct Costs			5,025,000	
	Soft Cost Contingency Allowance		5%	Other Indirect Costs			1,304,000	
	Total Indirect Costs							$27,387,000
IV.	**Financing Costs**							
	Interest During Construction							
	Land	[5]	$52,272,000	Cost	3.6%	Avg Rate	$2,823,000	
	Construction	[6]	$137,441,000	Cost	3.6%	Avg Rate	4,453,000	
	Loan Origination Fees		60%	Loan to Cost	2.0	Points	2,277,000	
	Total Financing Costs							$9,553,000
V.	**Total Construction Cost**		400	Units	$344,000	/Unit		$137,441,000
	Total Development Cost		400	Units	$474,000	/Unit		$189,713,000

[1] Estimated based on a survey of the sales between 2016 and 2018 of residentially zoned land.
[2] Based on the estimated costs for similar uses.
[3] Based on 1.0 spaces for Studio Units; 1.0 spaces for One-Bedroom Units; 2.0 spaces for Two-Bedroom Units; 2.5 spaces for Three-Bedroom Units; and 0.50 spaces per unit for guest parking.
[4] Based on estimates prepared for other projects within Huntington Beach.
[5] Based on an 18 month construction period and a 100% average outstanding loan balance.
[6] Based on an 18 month construction period and a 60% average outstanding loan balance.

APPENDIX A - EXHIBIT I - TABLE 2

ESTIMATED STABILIZED NET OPERATING INCOME
RENTAL APARTMENT DEVELOPMENT
10% INCLUSIONARY UNITS - MODERATE INCOME ALTERNATIVE
DENSITY @ 50 UNITS PER ACRE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

I.	**Gross Income**							
	A. Market Rate Units [1]							
	Studio Units	54	Units @	$2,652	/Unit/Month	$1,719,000		
	One-Bedroom Units	180	Units @	$3,189	/Unit/Month	6,888,000		
	Two-Bedroom Units	108	Units @	$4,856	/Unit/Month	6,293,000		
	Three-Bedroom Units	18	Units @	$5,501	/Unit/Month	1,188,000		
	B. Inclusionary Units: 10% of Units [2]							
	Studio Units	6	Units @	$1,932	/Unit/Month	139,000		
	One-Bedroom Units	20	Units @	$2,205	/Unit/Month	529,000		
	Two-Bedroom Units	12	Units @	$2,469	/Unit/Month	356,000		
	Three-Bedroom Units	2	Units @	$2,730	/Unit/Month	66,000		
	C. Laundry & Miscellaneous Income	400	Units @	$25	/Unit/Month	120,000		
	Total Gross Income						$17,298,000	
	Vacancy & Collection Allowance	5%	Gross Income				(865,000)	
II.	**Effective Gross Income**						$16,433,000	
III.	**Operating Expenses**							
	General Operating Expenses	400	Units @	$4,500	/Unit	$1,800,500		
	Property Taxes	400	Units @	$7,400	/Unit	2,949,000		
	Replacement Reserve Deposits	400	Units @	$150	/Unit	60,000		
	Total Operating Expenses						($4,809,500)	
IV.	**Stabilized Net Operating Income**						$11,623,500	

[1] Based on the rent survey undertaken in February 2020 and presented in APPENDIX C. The weighted average monthly rent equates to $4.01 per square foot of leasable area.

[2] The Inclusionary rent calculations are based on household income at 110% of AMI, with 30% of income allotted to housing related expenses. See APPENDIX D - EXHIBIT I.

APPENDIX A - EXHIBIT I - TABLE 3

ESTIMATED DEVELOPER RETURN
RENTAL APARTMENT DEVELOPMENT
10% INCLUSIONARY UNITS - MODERATE INCOME ALTERNATIVE
DENSITY @ 50 UNITS PER ACRE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

I.	**Stabilized Net Operating Income**	See APPENDIX A - EXHIBIT I - TABLE 2	$11,623,500
II.	**Total Development Cost**	See APPENDIX A - EXHIBIT I - TABLE 1	$189,713,000
III.	**Return on Total Investment**		6.1%

APPENDIX A - EXHIBIT II

RENTAL APARTMENT DEVELOPMENT
PRO FORMA ANALYSES
10% INCLUSIONARY UNITS - LOW INCOME ALTERNATIVE
DENSITY @ 50 UNITS PER ACRE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

APPENDIX A - EXHIBIT II - TABLE 1

ESTIMATED DEVELOPMENT COSTS
RENTAL APARTMENT DEVELOPMENT
10% INCLUSIONARY UNITS - LOW INCOME ALTERNATIVE
DENSITY @ 50 UNITS PER ACRE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

I.	**Property Acquisition Costs**	1	348,480	Sf of Land	$150	/Sf of Land		$52,272,000
II.	**Direct Costs**	2						
	On-Site Improvements/Landscaping		348,480	Sf of Land	$20	/Sf of Land	$6,970,000	
	Above-Ground Parking Spaces	3	750	Spaces	$25,000	/Space	18,750,000	
	Building Costs		464,250	Sf of GBA	$125	/Sf of GBA	58,031,000	
	Contractor/DC Contingency Allow		20%	Other Direct Costs			16,750,000	
	Total Direct Costs		464,250	Sf of GBA	$216	/Sf of GBA		$100,501,000
III.	**Indirect Costs**							
	Architecture, Engineering & Consulting		8%	Direct Costs			$8,040,000	
	Public Permits & Fees	4	400	Units	$20,000	/Unit	8,002,000	
	Taxes, Insurance, Legal & Accounting		3%	Direct Costs			3,015,000	
	Marketing		400	Units	$5,000	/Unit	2,001,000	
	Developer Fee		5%	Direct Costs			5,025,000	
	Soft Cost Contingency Allowance		5%	Other Indirect Costs			1,304,000	
	Total Indirect Costs							$27,387,000
IV.	**Financing Costs**							
	Interest During Construction							
	Land	5	$52,272,000	Cost	3.6%	Avg Rate	$2,823,000	
	Construction	6	$137,441,000	Cost	3.6%	Avg Rate	4,453,000	
	Loan Origination Fees		60%	Loan to Cost	2.0	Points	2,277,000	
	Total Financing Costs							$9,553,000
V.	**Total Construction Cost**		400	Units	$344,000	/Unit		$137,441,000
	Total Development Cost		400	Units	$474,000	/Unit		$189,713,000

1 Estimated based on a survey of the sales between 2016 and 2018 of residentially zoned land.
2 Based on the estimated costs for similar uses.
3 Based on 1.0 spaces for Studio Units; 1.0 spaces for One-Bedroom Units; 2.0 spaces for Two-Bedroom Units; 2.5 spaces for Three-Bedroom Units; and 0.50 spaces per unit for guest parking.
4 Based on estimates prepared for other projects within Huntington Beach.
5 Based on an 18 month construction period and a 100% average outstanding loan balance.
6 Based on an 18 month construction period and a 60% average outstanding loan balance.

APPENDIX A - EXHIBIT II - TABLE 2

ESTIMATED STABILIZED NET OPERATING INCOME
RENTAL APARTMENT DEVELOPMENT
10% INCLUSIONARY UNITS - LOW INCOME ALTERNATIVE
DENSITY @ 50 UNITS PER ACRE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

I.	**Gross Income**						
	A. Market Rate Units [1]						
	Studio Units	54	Units @	$2,652	/Unit/Month	$1,719,000	
	One-Bedroom Units	180	Units @	$3,189	/Unit/Month	6,888,000	
	Two-Bedroom Units	108	Units @	$4,856	/Unit/Month	6,293,000	
	Three-Bedroom Units	18	Units @	$5,501	/Unit/Month	1,188,000	
	B. Inclusionary Units: 10% of Units [2]						
	Studio Units	6	Units @	$1,031	/Unit/Month	74,000	
	One-Bedroom Units	20	Units @	$1,175	/Unit/Month	282,000	
	Two-Bedroom Units	12	Units @	$1,311	/Unit/Month	189,000	
	Three-Bedroom Units	2	Units @	$1,442	/Unit/Month	35,000	
	C. Laundry & Miscellaneous Income	400	Units @	$25	/Unit/Month	120,000	
	Total Gross Income						$16,788,000
	Vacancy & Collection Allowance	5%	Gross Income				(839,000)
II.	**Effective Gross Income**						$15,949,000
III.	**Operating Expenses**						
	General Operating Expenses	400	Units @	$4,500	/Unit	$1,800,500	
	Property Taxes	400	Units @	$7,100	/Unit	2,851,000	
	Replacement Reserve Deposits	400	Units @	$150	/Unit	60,000	
	Total Operating Expenses						($4,711,500)
IV.	**Stabilized Net Operating Income**						$11,237,500

1 Based on the rent survey undertaken in February 2020 and presented in APPENDIX C. The weighted average monthly rent equates to $4.01 per square foot of leasable area.

2 The Inclusionary rent calculations are based on household income at 60% of AMI, with 30% of income allotted to housing related expenses. See APPENDIX D - EXHIBIT I.

APPENDIX A - EXHIBIT II - TABLE 3

INCLUSIONARY HOUSING IMPACTS
RENTAL APARTMENT DEVELOPMENT
10% INCLUSIONARY UNITS - LOW INCOME ALTERNATIVE
DENSITY @ 50 UNITS PER ACRE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

I.	**Supportable Investment**				
	Stabilized Net Operating Income	See APPENDIX A - EXHIBIT II - TABLE 2	$11,237,500		
	Threshold Return on Total Investment [1]		6.1%		
	Total Supportable Investment			$183,413,000	
II.	**Total Development Cost**	See APPENDIX A - EXHIBIT II - TABLE 1		$189,713,000	
III.	**Reduced Value**				($6,300,000)
	Return on Total Investment				5.9%

[1] Based on the Developer Return estimated to be generated by the DENSITY @ 50 UNITS PER ACRE: MODERATE INCOME ALTERNATIVE.

APPENDIX A - EXHIBIT III

RENTAL APARTMENT DEVELOPMENT
PRO FORMA ANALYSES
10% INCLUSIONARY UNITS - VERY LOW INCOME ALTERNATIVE
35% DENSITY BONUS: 67.5 UNITS PER ACRE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

APPENDIX A - EXHIBIT III - TABLE 1

ESTIMATED DEVELOPMENT COSTS
RENTAL APARTMENT DEVELOPMENT
10% INCLUSIONARY UNITS - VERY LOW INCOME ALTERNATIVE
35% DENSITY BONUS: 67.5 UNITS PER ACRE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

I.	**Property Acquisition Costs**	[1]	348,480	Sf of Land	$150	/Sf of Land		$52,272,000
II.	**Direct Costs**	[2]						
	On-Site Improvements/Landscaping		348,480	Sf of Land	$20	/Sf of Land	$6,970,000	
	Above-Ground Parking Spaces	[3]	729	Spaces	$25,000	/Space	18,225,000	
	Building Costs		626,738	Sf of GBA	$150	/Sf of GBA	94,011,000	
	Contractor/DC Contingency Allow		20%	Other Direct Costs			23,841,000	
	Total Direct Costs		626,738	Sf of GBA	$228	/Sf of GBA		$143,047,000
III.	**Indirect Costs**							
	Architecture, Engineering & Consulting		8%	Direct Costs			$11,444,000	
	Public Permits & Fees	[4]	540	Units	$20,000	/Unit	10,800,000	
	Taxes, Insurance, Legal & Accounting		3%	Direct Costs			4,291,000	
	Marketing		540	Units	$5,000	/Unit	2,700,000	
	Developer Fee		5%	Direct Costs			7,152,000	
	Soft Cost Contingency Allowance		5%	Other Indirect Costs			1,819,000	
	Total Indirect Costs							$38,206,000
IV.	**Financing Costs**							
	Interest During Construction							
	Land	[5]	$52,272,000	Cost	3.6%	Avg Rate	$2,823,000	
	Construction	[6]	$193,285,000	Cost	3.6%	Avg Rate	6,262,000	
	Loan Origination Fees		60%	Loan to Cost	2.0	Points	2,947,000	
	Total Financing Costs							$12,032,000
V.	**Total Construction Cost**		540	Units	$358,000	/Unit		$193,285,000
	Total Development Cost		540	Units	$455,000	/Unit		$245,557,000

[1] Estimated based on a survey of the sales between 2016 and 2018 of residentially zoned land.
[2] Based on the estimated costs for similar uses.
[3] Based on 1.0 space for Studio Units; 1.0 space for One-Bedroom Units; 2.0 spaces for Two-Bedroom Units; and 2.5 space for Three-Bedroom Units. No guest spaces are provided.
[4] Based on estimates prepared for other projects within Huntington Beach.
[5] Based on an 18 month construction period and a 100% average outstanding loan balance.
[6] Based on an 18 month construction period and a 60% average outstanding loan balance.

APPENDIX A - EXHIBIT III - TABLE 2

ESTIMATED STABILIZED NET OPERATING INCOME
RENTAL APARTMENT DEVELOPMENT
10% INCLUSIONARY UNITS - VERY LOW INCOME ALTERNATIVE
35% DENSITY BONUS: 67.5 UNITS PER ACRE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

I.	**Gross Income**						
	A. Market Rate Units [1]						
	Studio Units	74	Units @	$2,652	/Unit/Month	$2,355,000	
	One-Bedroom Units	248	Units @	$3,189	/Unit/Month	9,490,000	
	Two-Bedroom Units	149	Units @	$4,856	/Unit/Month	8,682,000	
	Three-Bedroom Units	25	Units @	$5,501	/Unit/Month	1,650,000	
	B. Density Bonus: 11% Base Zoning Units [2]						
	Studio Units	7	Units @	$850	/Unit/Month	71,000	
	One-Bedroom Units	22	Units @	$969	/Unit/Month	256,000	
	Two-Bedroom Units	13	Units @	$1,079	/Unit/Month	168,000	
	Three-Bedroom Units	2	Units @	$1,185	/Unit/Month	28,000	
	C. Laundry & Miscellaneous Income	540	Units @	$25	/Unit/Month	162,000	
	Total Gross Income						$22,862,000
	Vacancy & Collection Allowance	5%	Gross Income				(1,143,000)
II.	**Effective Gross Income**						$21,719,000
III.	**Operating Expenses**						
	General Operating Expenses	540	Units @	$4,500	/Unit	$2,430,000	
	Property Taxes	540	Units @	$7,200	/Unit	3,887,000	
	Replacement Reserve Deposits	540	Units @	$150	/Unit	81,000	
	Total Operating Expenses						($6,398,000)
IV.	**Stabilized Net Operating Income**						$15,321,000

[1] Based on the rent survey undertaken in February 2020 and presented in APPENDIX C. The weighted average monthly rent equates to $4.01 per square foot of leasable area.

[2] The Inclusionary rent calculations are based on household income at 50% of AMI, with 30% of income allotted to housing related expenses. See APPENDIX D - EXHIBIT I.

APPENDIX A - EXHIBIT III - TABLE 3

INCLUSIONARY HOUSING IMPACTS
RENTAL APARTMENT DEVELOPMENT
10% INCLUSIONARY UNITS - VERY LOW INCOME ALTERNATIVE
35% DENSITY BONUS: 67.5 UNITS PER ACRE
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

I.	**Supportable Investment**				
	Stabilized Net Operating Income	See APPENDIX A - EXHIBIT III - TABLE 2	$15,321,000		
	Threshold Return on Total Investment [1]		6.1%		
	Total Supportable Investment			$250,062,000	
II.	**Total Development Cost**	See APPENDIX A - EXHIBIT III - TABLE 1		$245,557,000	
III.	**Enhanced Value**				$4,505,000
	Return on Total Investment				6.2%

[1] Based on the Developer Return estimated to be generated by the DENSITY @ 50 UNITS PER ACRE: MODERATE INCOME ALTERNATIVE.

APPENDIX B

RENTAL APARTMENT DEVELOPMENT
AFFORDABILITY ANALYSES
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

APPENDIX D - EXHIBIT I

AFFORDABLE RENT CALCULATIONS
2020 INCOME STANDARDS
RENTAL APARTMENT DEVELOPMENT
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

			Studio Units	One-Bedroom Units	Two-Bedroom Units	Three-Bedroom Units
I.	**General Assumptions**					
	Area Median Income (AMI)	[1]	$72,100	$82,400	$92,700	$103,000
	Monthly Utilities Allowance	[2]	$51	$61	$80	$103
II.	**Affordable Rent Calculations**	[3]				
	A. Moderate Income - Rent Based on 110% AMI					
	Benchmark Annual Household Income		$79,310	$90,640	$101,970	$113,300
	Percentage of Income Allotted to Housing Expenses		30%	30%	30%	30%
	Monthly Income Available for Housing Expenses		$1,983	$2,266	$2,549	$2,833
	(Less) Monthly Utilities Allowance		(51)	(61)	(80)	(103)
	Maximum Allowable Rent		$1,932	$2,205	$2,469	$2,730
	B. Low Income - Rent Based on 60% AMI					
	Benchmark Annual Household Income		$43,260	$49,440	$55,620	$61,800
	Percentage of Income Allotted to Housing Expenses		30%	30%	30%	30%
	Monthly Income Available for Housing Expenses		$1,082	$1,236	$1,391	$1,545
	(Less) Monthly Utilities Allowance		(51)	(61)	(80)	(103)
	Maximum Allowable Rent		$1,031	$1,175	$1,311	$1,442
	C. Very Low Income - Rent Based on 50% AMI					
	Benchmark Annual Household Income		$36,050	$41,200	$46,350	$51,500
	Percentage of Income Allotted to Housing Expenses		30%	30%	30%	30%
	Monthly Income Available for Housing Expenses		$901	$1,030	$1,159	$1,288
	(Less) Monthly Utilities Allowance		(51)	(61)	(80)	(103)
	Maximum Allowable Rent		$850	$969	$1,079	$1,185

[1] Based on the 2020 Orange County household incomes published by the California Housing & Community Development Department (HCD). The benchmark household size is set at the number of bedrooms in the unit plus one.

[2] Based on the Orange County Housing Authority utility allowance schedule effective as of 10/1/19. Assumes: Gas Cooking, Gas Heating, and Gas Water Heater; and Basic Electric.

[3] Based on the California Health & Safety Code Section 50053 calculation methodology.

APPENDIX D - EXHIBIT II

IN-LIEU FEE ANALYSIS
RENTAL APARTMENT DEVELOPMENT
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

			Moderate Income	Low Income
I.	**Rent Difference**	1		
A.	**Studio Units**			
	Market Rate Units		$2,652	$2,652
	Affordable Units		1,932	1,031
	Difference		$720	$1,622
B.	**One-Bedroom Units**			
	Market Rate Units		$3,189	$3,189
	Affordable Units		2,205	1,175
	Difference		$984	$2,014
C.	**Two-Bedroom Units**			
	Market Rate Units		$4,856	$4,856
	Affordable Units		2,469	1,311
	Difference		$2,387	$3,545
D.	**Three-Bedroom Units**			
	Market Rate Units		$5,501	$5,501
	Affordable Units		2,730	1,442
	Difference		$2,772	$4,059
II.	**Distribution of Total Units**	2		
	Studio Units		15%	15%
	One-Bedroom Units		50%	50%
	Two-Bedroom Units		30%	30%
	Three-Bedroom Units		5%	5%
III.	**Annual Affordability Gap Per Affordable Unit**		$17,455	$30,201
	Less: Property Tax Difference	3	(4,430)	(7,660)
	Annual Affordability Gap Per Affordable Unit		$13,025	$22,541
IV.	**Net Affordability Gap Per Affordable Unit**	4	$192,000	$332,000
V.	**In-Lieu Fee**			
	Per Total Unit	5	$19,200	$33,200
	Per Square Foot of Net Leasable Area	6	$20.70	$35.80

1 The market rents are drawn from the pro forma analyses. See APPENDIX D - EXHIBIT I: The affordable rents are based on the H&SC Section 50053 calculation methodology.
2 Based on the unit mix distribution applied in the pro forma analysis.
3 Based on the rent differential capitalized at a 4.3% rate to establish the value, and a 1.1% property tax rate.
4 Based on the Annual Affordability Gap Per Affordable Unit capitalized at the Threshold Return on Total Investment.
5 Based on the Affordability Gap Per Affordable Unit multiplied times the total number of units in the project.
6 Based on the Affordability Gap Per Affordable Unit divided by the average net leasable area per unit.

APPENDIX C

RENTAL APARTMENT DEVELOPMENT
RENT SURVEY
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

APPENDIX C

RENT SURVEY - 4 STAR PROPERTIES
RENTAL APARTMENT DEVELOPMENT
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

Name	Address	# of Units	Unit Size (SF)	Average Effective Rent Total	Average Effective Rent Per SF	Parking Spaces Provided Per Unit	Year Built
		Studio Units					
Elan Huntington Beach	18504 Beach Boulevard	73	576	$2,464	$4.28	1.1	2015
The Residences at Bella Terra	7521 Edinger Avenue	67	585	$1,844	$3.15	1.1	2013
Beach & Ocean	19891-19895 Beach Boulevard	28	608	$2,035	$3.35		2014
Avalon Huntington Beach	7400 Center Avenue	62	690	$2,061	$2.99		2016
LUCE	7290 Edinger Avenue	26	670	$1,998	$2.98	1.7	2018
	Minimum		576	$1,844	$2.98		
	Maximum		690	$2,464	$4.28		
	Weighted Average		619	$2,110	$3.44		
		One-Bedroom Units					
The Residences at Bella Terra	7521 Edinger Avenue	212	773	$2,187	$2.83		
LUCE	7290 Edinger Avenue	245	807	$2,337	$2.90		
Elan Huntington Beach	18504 Beach Boulevard	126	784	$2,101	$2.68		
Avalon Huntington Beach	7400 Center Avenue	196	777	$2,295	$2.95		
Beach & Ocean	19891-19895 Beach Boulevard	91	687	$2,355	$3.43		
Residences at Pacific City	21034 Pacific Coast Highway	306	944	$3,671	$3.89		
	Minimum		687	$2,101	$2.68		
	Maximum		944	$3,671	$3.89		
	Weighted Average		820	$2,626	$3.17		

Source: Costar; February 2020
Prepared by: Keyser Marston Associates, Inc.
File name: HB Rent Inclusionary 5 6 20

APPENDIX C

RENT SURVEY - 4 STAR PROPERTIES
RENTAL APARTMENT DEVELOPMENT
FINANCIAL ANALYSIS: INCLUSIONARY HOUSING ORDINANCE UPDATE
HUNTINGTON BEACH, CALIFORNIA

Name	Address	# of Units	Unit Size (SF)	Average Effective Rent Total	Average Effective Rent Per SF	Parking Spaces Provided Per Unit	Year Built
			Two-Bedroom Units				
LUCE	7290 Edinger Avenue	219	1,142	$2,834	$2.48		
The Residences at Bella Terra	7521 Edinger Avenue	146	1,170	$2,776	$2.37		
Elan Huntington Beach	18504 Beach Boulevard	75	1,104	$2,644	$2.39		
Beach & Ocean	19891-19895 Beach Boulevard	54	980	$2,939	$3.00		
Avalon Huntington Beach	7400 Center Avenue	120	1,191	$3,035	$2.55		
Residences at Pacific City	21034 Pacific Coast Highway	96	1,279	$5,354	$4.19		
	Minimum		980	$2,644	$2.37		
	Maximum		1,279	$5,354	$4.19		
	Weighted Average		1,158	$3,185	$2.73		
			Three-Bedroom Units				
The Residences at Bella Terra	7521 Edinger Avenue	42	1,497	$3,416	$2.28		
LUCE	7290 Edinger Avenue	20	1,446	$3,754	$2.60		
Residences at Pacific City	21034 Pacific Coast Highway	114	1,593	$5,654	$3.55		
	Minimum		1,446	$3,416	$2.28		
	Maximum		1,593	$5,654	$3.55		
	Weighted Average		1,553	$4,904	$3.14		

Source: Costar; February 2020
Prepared by: Keyser Marston Associates, Inc.
File name: HB Rent Inclusionary 5 6 20