

Draft Report

Ownership Inclusionary Housing In-Lieu Fee

The Economics of Land Use



Prepared for:

City of Foster City

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EXECUTIVE SUMMARY

Economic & Planning Systems, Inc. (EPS) was hired by the City of Foster City to create new affordable housing fees, including the inclusionary housing in-lieu fee. The City is currently considering an inclusionary housing ordinance under which 20 percent of units in a home-ownership project would be required to be offered at below-market-rate prices affordable to “moderate income” households earning up to 110 percent of the Area Median Income as established by the State of California’s Department of Housing and Community Development (HCD).

Table 1, below, shows the in-lieu fee calculation results. As detailed later in this document, the in-lieu fees are based on the aggregate subsidy required to produce the number of affordable units prescribed under the inclusionary housing ordinance (20 affordable units out of each 100 total units in a project). As shown, the fee associated with the 20 percent inclusionary requirement (moderate income) is calculated to be \$83,548 per market-rate unit, or \$48.21 per square foot of the market-rate homes. Adopting fees at these levels would represent the true costs of the City’s inclusionary housing ordinance, as the calculations are based on the costs versus values of units meeting the inclusionary ordinance. As such, fees at this level would represent a generally “cost-neutral” option to developers relative to producing inclusionary units within their projects.

Table 1 Summary of In-Lieu Fees for Home-Ownership Projects

Item	Income Level		In-Lieu Fee		
	Moderate (110% AMI)	Total	per Affordable Unit	per Market- Rate Unit	per Market- Rate Square- foot [1]
Units	20	20	20	100	
Value/Unit	\$907,946				
Total Value	\$18,158,920	\$18,158,920			
Costs/Unit	\$1,325,687				
Total Costs	\$26,513,745	\$26,513,745			
Subsidy per Unit	\$417,741				
Total Subsidy Required	\$8,354,825	\$8,354,825	\$417,741	\$83,548	\$48.21

[1] Consistent with the affordability gap analysis, an average unit size of 1,733 square feet is assumed. This area is the average unit size of townhomes sold in Foster City over the last five years.

Source: CoStar; San Mateo County; Economic & Planning Systems, Inc.

METHODOLOGY

Through an affordability gap analysis, this report estimates the subsidy needed to produce for-sale housing that is affordable to moderate-income households in the event that developers do not build the units themselves. Under separate covers, EPS has produced an in-lieu fee calculation for rental projects, and a memorandum reflecting comparable jurisdictions and feasibility findings.

Maximum Affordable Housing Income Levels

The City is exploring an inclusionary housing ordinance that would require that for-sale development provide 20 percent of all new units at prices affordable at “moderate” income levels. The income levels are set for the County of San Mateo by the California Department of Housing and Community Development (HCD) on an annual basis. **Table 2** shows the income limits for 2021, which vary by the number of people in the household. Based on recent ownership developments and input from City staff, EPS assumed the average unit in a typical for-sale development would be three-bedrooms serving a four-person household. Thus, **Table 2** illustrates the income limits for a four-person household for San Mateo County. The Area Median Income for a family of four in San Mateo County is \$149,600 in 2021 as shown below. Please note that the nominal income categories do not necessarily correspond mathematically to the figures set by HCD; for example, “low” income is nominally meant to represent households earning up to 80 percent of median income, but in San Mateo County the maximum income allowed by HCD in this category is nearly 100 percent of median income.

Table 2 San Mateo County 2021 Income Limits for 4-Person Households

Income Group and Definition		2021 Maximum Income 4-Person Household
Extremely Low	≤30% AMI	\$54,800
Very Low	>30% to ≤50% AMI	\$91,350
Low	>50% to ≤80% AMI	\$146,350
Median (Base)	>80% to ≤100% AMI	\$149,600
Moderate	>100% AMI to ≤120% AMI	\$179,500

Source: San Mateo County 2021 Income Limits, California Housing and Community Development (HCD).

Affordability Gap Analysis

Product Type

The analysis assumes that moderate-income households would be housed in affordable units similar to the type of ownership construction currently observed in the City. The assumed prototype reflects townhome construction at 17 dwelling units to the acre, which City staff has confirmed as a representative prototype of housing developments they expect to be built.

California State law (California Health and Safety Code Section 50052.5) assumes that a 3-bedroom unit is occupied by a 4-person household, and this assumption is used in this analysis. Consistent with input from the City and data gathered from Zillow and other online sources regarding recently constructed projects, EPS assumes that the typical unit size is 1,733 square feet.

Development Cost Assumptions

Affordable housing development costs include land costs, direct costs (e.g., labor and materials), and indirect or “soft” costs (e.g., architecture and engineering, entitlement, marketing, etc.). In addition, a developer must achieve a profit margin in order to justify their investment and risk. Data from recent developments and recent land transactions within Foster City have been combined with EPS’s information from various market-rate and affordable housing developers on the Peninsula to estimate appropriate development cost assumptions for use in Foster City. These assumptions are shown on **Table 4** and indicate that the total cost per unit for a for-sale townhome is about \$1.3 million. By necessity, this figure represents a “prototypical” project; the actual costs for a given project will vary by location and project design characteristics.

Revenue Assumptions

To calculate the values of the affordable units, assumptions must be made regarding the applicable income level and the percentage of household income spent on housing costs. The following assumptions were used in these calculations:

- *Income Levels*—This analysis estimates the subsidy required to produce units for four-person households at HCD-defined income levels as shown in **Table 2**. As is customary among jurisdictions that require moderate-income ownership units, EPS has calculated the affordable price assuming the household earns 110 percent of median income, though the nominal “moderate income” category could reach as high as 120 percent of median income. This assumption parallels State law regarding the use of density bonuses for moderate income households, and reflects the idea that the units should not be affordable only to those households earning literally the maximum figure allowed in the income category.
- *Percentage of Gross Household Income Available for Housing Costs*—HCD standards on overpaying for housing indicate that moderate income households should pay no more than 35 percent of their gross income on housing costs.
- *Housing Costs Included for For-Sale Units*—Ownership housing costs include mortgage principal and interest, plus estimates of annual Homeowners Association (HOA) fees and insurance costs, estimated private mortgage insurance payments, and property taxes. The analysis assumes a 30-year fixed mortgage with a 3.5 percent effective interest rate, plus a 10 percent down payment from the homebuyer.

Affordability Gap Results

Table 4 shows the subsidies required for construction of townhome units for four-person households earning 110 percent of median income. As shown, such households would earn \$164,550 annually and could afford to pay up to roughly \$908,000 for a home. However, such homes are estimated to cost over \$1.3 million to develop, thus requiring a subsidy of \$418,000.

Table 3 Affordability Gap Analysis

Item	Townhomes Moderate Income (110% AMI)
Development Program Assumptions	
Density/Acre	17
Net Unit Size	1,733
Number of Bedrooms per Unit	3
Number of Persons per Unit [1]	4
Cost Assumptions	
Land/Acre [2]	\$7,837,315
Land/Unit	\$461,019
Direct Costs	
Direct Construction Costs/Gross SF [3]	\$300
Direct Construction Costs/Unit	\$519,900
Parking Construction Costs/Space	Included
Parking Construction Costs/Unit	Included
Subtotal, Direct Costs/Unit	\$519,900
Indirect Costs as a % of Direct Costs [4]	35%
Indirect Costs/Unit	\$181,965
Developer Fee (% of all costs)	14%
Developer Fee	\$162,804
Cost w/o Developer Fee	\$1,162,884
Total Cost/Unit (rounded)	\$1,325,687
Maximum Supported Home Price	
Household Income [5]	\$164,550
Monthly Payments [6]	\$4,799
Mortgage Terms	
Insurance	\$125
Taxes	\$755
HOA	\$250
Down Payment	10%
Interest Rate	0.29%
Loan Term (months)	360
Sales Price [7]	\$907,946
Affordability Gap	(\$417,741)

[1] For this analysis, EPS has assumed an average unit for income-qualified worker households would be 3-bedrooms. State law (Health and Safety Code Section 50052.5) indicates that a 3-bedroom unit should be assumed to be occupied by a 4-person household.

[2] Based on CoStar reported land sale transactions in Foster City.

[3] Includes costs for parking, contingency, and site improvement.

[4] Includes costs for architecture and engineering; entitlement and fees; project management; appraisal and market study; marketing, commissions, and general administration; financing and charges; and insurance.

[5] Based on 2021 income limits for a four-person household in San Mateo County.

[6] Assumes housing costs (e.g., mortgage payments and utilities) to be 35% of gross household income for Moderate incomes.

[7] Based on the assumed housing costs and present values given the mortgage terms.

Source: CoStar; California Department Housing and Community Development; Economic & Planning Systems, Inc.

In-Lieu Fee Calculations

Table 5 then translates these subsidies into in-lieu fees. A prototypical 100-unit ownership project would be required to provide fees sufficient to subsidize 20 moderate (110) income units, which would cost \$26.5 million to build but would only be worth \$18 million total or about \$908,000 per affordable unit. The difference, roughly \$8.35 million, represents the subsidy that the 100-unit market-rate project would need to provide via in-lieu fees, translating to a fee of \$83,548 per market-rate unit or \$48.21 per market-rate square-foot.

Table 4 In-Lieu Fee Calculation

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Source: CoStar; San Mateo County; Economic & Planning Systems, Inc.

While it is useful to think of the total in-lieu fee as it may apply to each market-rate unit, it is also useful to know the fee per affordable unit, as some projects will be required to provide a certain number of units but may be allowed to meet any fractional obligation through payment of a fee. For example, under the current inclusionary housing ordinance, which requires 20 percent inclusionary units, a 117-unit project would be required to provide 23.4 affordable units. If 23 units are provided on site, the additional 0.4-unit requirement could be met by charging a fee of 0.4 times the \$417,741 per affordable unit fee, or a total payment of \$167,096.