FROM	
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AGENCY NAME & ADDRESS	Bureau of the Budget and Management Research Room 432, City Hall
SUBJECT	City Council Bill 22-0195 – Inclusionary Housing

CITY of BALTIMORE

MEMO

TO

The Honorable President and
Members of the City Council
City Hall, Room 400

DATE: November 17, 2022

Position: Oppose

The Department of Finance is herein reporting on City Council Bill 22-0195, Inclusionary Housing for Baltimore City, the purpose of which is to provide rules and regulations for developers on inclusionary housing requirements for new developments.

Background

In 2007, the City enacted Ordinance 07-474, Inclusionary Housing, with the intent of encouraging economic diversity across City neighborhoods by providing affordable rental and homeownership opportunities in communities experiencing an increase in market-rate housing without imposing financial burdens on developers. However, due to the complexities of the Ordinance, only 34 affordable have been built since 2007 from the law. In 2020, legislation extended the program by two years from 2020 to 2022, but the program expired on June 30, 2022.

This legislation would require developers to create affordable units as part of any new residential project. It would apply to any residential project that is newly-constructed, wholly renovated, or converted, with at least 20 units and a cost of at least $60,000 per unit. The “affordable” requirement would equal 10% of total units, with half required to be set aside for those with incomes at 50-80% of the Area Median Income (AMI).

Concurrent to this legislation, the Department of Housing and Community Development (DHCD) issued an RFP to seek a consultant to assist with updating the Inclusionary Housing Ordinance. Enterprise Community Partners was chosen as the consultant and completed a draft report in August 2021 and final report in November 2022.

Fiscal Impact

The Department of Finance anticipates the need for major City investments to support the implementation of development projects as a result of this legislation.

For an inclusionary housing program to be successful without having a negative impact on the housing market, one of two things must be in place. First, there must be such strong demand for market-rate development that developers will build even with the additional costs from the inclusionary requirements. Or, second, the City must provide a subsidy to developers to compensate for the additional costs.

To evaluate the first condition, Enterprise performed a market analysis to understand where market-rate development is occurring in the City and if the market could absorb an inclusionary requirement. Enterprise defined three sub-markets for evaluating market strength:

- Core Sub-Markets: This represents locations where the majority of new market-rate development is occurring today and prices are the highest. It includes a small sliver of locations along the Harbor and adjacent to downtown. Recently built multi-family units in the "Core" sub-market include 414 Light Street (Otterbein), Banner Hill Apartments (Otterbein), Bainbridge Federal Hill (Federal Hill), Avalon 555 President (Inner Harbor), and 1405 Point (Harbor Point / Fells Point).
- Strong Sub-Markets: This includes the remaining markets in Baltimore that have the potential to support new market-rate development today. Recently built multi-family units in the "Strong" sub-market include The Woodberry (Woodberry), ICON Residences at the Rotunda (Hampden), Remington Row (Remington), 225 North Calvert (Downtown), and 101 Ellwood (Patterson Park).
- Transitional Sub-Markets: This includes areas that are maturing and could support market-rate development in the future.

Next, Enterprise analyzed how the potential enactment of an inclusionary housing policy could impact the feasibility of development in each of these sub-markets. Enterprise modeled a sample project in each sub-market for both a new construction project and a rehab project. They also assumed that new projects would receive the High-Performance Market Rate Tax Credit, since that incentive is available to most new development of market-rate multi-family buildings in Baltimore. The High-Performance Market Rate Tax Credit provides an 80% property tax abatement in years one through five, then declining by 10% each year until reaching 30% tax abatement in year ten.

In both the Strong and Transitional sub-markets, for both mid-rise new construction and rehabs, Enterprise determined that multi-family developments are infeasible. This means that the revenue generated from these projects is not enough to cover the costs for developing and operating the property. Any further inclusionary requirements, such as those required by this legislation, would make those projects even more infeasible and in practice could limit the construction of multi-family housing in those sub-markets.

In the Core sub-market, Enterprise estimated that market-rate development is feasible but only at very narrow profit margins. Enterprise tested ten potential inclusionary housing requirements at various levels of AMI. Nine of the ten scenarios tested were infeasible, with only one scenario (5% affordable requirement for 80% AMI) as feasible. The conclusion is that even in the Core sub-market, an additional 15% tax abatement on top of the High-Performance Market Rate Tax Credit would be required to ensure feasibility for projects with varying affordable housing requirements.

Although the 15% tax abatement proposal is not included in this legislation, Finance produced an estimate of this proposal to demonstrate the cost of a City subsidy to support inclusionary housing. The Enterprise report proposed adding an additional 15% abatement to each year of the current High-Performance Market Rate Tax Credit, which would increase the abatement as follows:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Year 6**	**Year 7**	**Year 8**	**Year 9**	**Year 10**
Current Abatement	80%	80%	80%	80%	80%	70%	60%	50%	40%	30%
Proposed Abatement	95%	95%	95%	95%	95%	85%	75%	65%	55%	45%

To determine the cost of the additional subsidy, Finance looked at projects that qualified for the High-Performance Market Rate Tax Credit over the last 10 years from Fiscal 2014 through Fiscal 2023. An additional 15% subsidy for 20 projects in the "Core" sub-market would have cost the City an additional **$9.9 million** and produced only 349 affordable additional units:

Number of Projects in "Core" Sub-Market	20
Additional HPMRTC Cost	$9.9 million
Total Number of Units Produced	3,497
Total Number of Affordable Units (at 10%)	349
City Cost per Affordable Unit	$28,493

A more cost-effective alternative to offering direct City subsidies is to offer other non-cash provisions to developers that meet the inclusionary requirements. Examples of these provisions include reducing parking requirements or removing height limits on new buildings. Presumably, these types of provisions could reduce the cost of development and make projects on the margins more financially feasible.

Conclusion

The Department of Finance supports the intent of this legislation, but does not believe that the City can support a broad-based inclusionary housing requirement as envisioned. The Enterprise report, which was commissioned to study this issue, concludes that market-rate multi-housing family development for the vast majority of the City is already financially challenging even before adding in new inclusionary housing requirements. And, even in the highest-priced sub-markets, some financial support would be required to support these new inclusionary requirements. Offering a City subsidy, as suggested in the Enterprise report, would pull valuable tax revenue away from other important City priorities and investments.

The City is still in a precarious overall position, with high numbers of vacant properties, a declining population, and a variety of social challenges. Although this inclusionary housing proposal is well-intentioned, Finance is concerned that in practice it could repel additional investment in Baltimore which is much-needed at this juncture of the City's history. Finance would recommend significantly limiting the scope of this legislation to the narrow "Core" sub-market cited in the Enterprise report, and to seek non-subsidy options for designing such a program.

For the reasons stated above, the Department of Finance opposes City Council Bill 22-0195.

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