



MEMORANDUM

STEPHANIE
RAWLINGS-BLAKE,
Mayor

PAUL T. GRAZIANO,
Executive Director, HABC
Commissioner, HCD

To: The Honorable President and Members of the Baltimore City Council
c/o Karen Randle, *Executive Secretary*

From: Paul T. Graziano, *Commissioner*

Date: September 18, 2012

Re: **City Council Bill 12-0066 – Report on the Applicability of the Inclusionary Housing Requirements**



INTRODUCTION

At the hearing of the Taxation, Finance and Economic Development Committee of the Baltimore City Council held on July 11, 2012, Department of Housing and Community Development (“HCD”) staff presented initial conclusions related to Inclusionary Housing (“IH”) requirements for the project known as “Lexington Square.” The development is before the City Council in conjunction with City Council Bill 12-0066, which provides for a Payment In Lieu of Taxes (“PILOT”) to support the project. At that time, Chairman Stokes requested additional written analysis of the application of the application of the Inclusionary Housing ordinance, which is codified at Article 13, Subtitle 2B of the Baltimore City Code, to the Lexington Square project.

If the proposed PILOT is passed and approved by the Board of Estimates, Lexington Square project will be subject to the Inclusionary Housing ordinance.

Under the Inclusionary Housing ordinance, when a PILOT is provided, twenty percent of the units in the development must be affordable for households at certain specified income ranges between 30% and 120% of the area median income. The City is obligated to provide subsidies to offset any financial impact to the developer caused by providing these units at below-market rates. If the public subsidy provided by the PILOT cannot be increased to offset the financial impact on the developer of providing the required number of affordable units the City may grant a cash subsidy to the developer to offset the financial impact of providing the units. If the Housing Commissioner determines that neither the PILOT nor a cash subsidy are sufficient to offset the financial impact of providing the affordable units, then the Housing Commissioner shall exempt the project from the Inclusionary Housing law or modify the number of affordable units required. Furthermore, there are provisions for waiving the requirements if the units to be provided exceed certain threshold costs.

For the reasons set forth below, HCD believes that the Housing Commissioner must exempt Lexington Square from the requirements of the Inclusionary Housing law. However, HCD, BDC and the development team have been working in good faith to develop a program of voluntary compliance. This voluntary program is in keeping with the spirit of the law, but will be the full responsibility of the development team.

Comments

ANALYSIS OF INCLUSIONARY HOUSING LAW WAIVER REQUIREMENTS

HCD has undertaken a thorough fiscal analysis (see: “Attachment ‘A’”) and determined that the Inclusionary Housing law adds an additional \$9,449,059 to the total overall cost to the project.

Several provisions¹ of the Inclusionary Housing law require that the City exempt/waive the project from the Inclusionary Housing requirements if the financial impact cannot be offset. Additionally, there are provisions with respect to unit cost in § 2B-21(f) which require the City to exempt the project if cost of providing the units exceeds certain thresholds.

The Inclusionary Housing law applies a three-part waiver test in determining whether the Commissioner is required by the law to exempt the project from its applicability, the prongs of which are addressed, in turn, below:

1) Waivers for Funding

Currently, BDC and HCD project that the PILOT proposed for this project, if increased to the legal maximum allowed under State and City law, would generate an additional \$1.2 million in public subsidy.

An alternative to funding the cost offset with the Major Public Subsidy is to provide cash to the developer. However, there are no uncommitted funds currently available in the Inclusionary Housing Offset Fund (which was originally appropriated only \$2 million). HCD has spent or obligated the full amount available for other Inclusionary Housing projects since the Fund’s creation in 2007. Currently the Fund has only \$520,000 available, and all those funds are dedicated to other projects. HCD does not have other sources of funds available to provide the cost offset.

As a result, HCD has determined that section 2B-21(d)(1)(i) applies and that the Housing Commissioner must exempt the project from the inclusionary housing law.

2) Waiver for Threshold

Section 2B-21(f), identifies ‘investment threshold’ as a cause for waiving the Inclusionary Requirements. The law places maximum financial impact levels per income tier and requires that the Commissioner must exempt projects for which the units exceed the thresholds.

The thresholds are as follows:

Chart 1: Investment Thresholds by Income Tier

Income Tier	30% AMI	60% AMI	80% AMI	100% AMI
Amount	\$125,000	\$100,000	\$50,000	\$25,000

Comparing these thresholds to the per unit costs identified in Chart 7² shows that nearly every category of unit type is over the threshold limit. The only category not over is 1-bedroom, 100% AMI units. The

¹ Article 13, § 2B-4(f); § 2B-6(a),(b) and (c); and § 2B-21(d)

² See, “Attachment ‘A’”, *infra*, at page 7.

maximum rent for those units (\$1605.00) exceeds the projected market rate rent for the building in the first year of operation and there is no 'gap' on which to base the financial impact calculation.

The requirement of this section, 2B-21(f)(3), is that the Commissioner must exempt the project from the applicability of the Inclusionary Housing law and shall "require that the developer deposit into the Inclusionary Housing Offset Fund an amount equal to the lesser of the following amounts, but only if the major public subsidy has been increased to fully offset the cost to the developer of making the deposit." The amounts contemplated by this section are the lower of: (1) the threshold amounts for all the units in the project that would be inclusionary; or (2) 20% of the total cost of providing the full offset.

For this project those amounts are (1) \$4,736,000 or (2) \$1,889,811.87. The latter is the lower value and the law requires that the developer make a deposit of \$1,889,811.87 to the IH Offset Fund but only if "the major public subsidy has been increased to fully offset the cost." As has been previously discussed, the maximum increase in major public subsidy (the PILOT) is \$1.2 million, less than the amount of the required deposit, and so the developer is waived by section 2B-21(f)(3)(ii) from this requirement as well.

This section does not allow for a partial waiver or adjustment of income tiers, only a reduction in the payment to the IH Offset Fund based on how much additional major public subsidy is made available by the City.

3) Waiver for Modified Requirements – Housing Commissioner

Section 2B-21(d)(1)(ii) allows the Commissioner to modify the requirements of the Inclusionary Housing Law by reducing the overall number of units required such that the amount of available subsidy is sufficient to cover the financial impact of the new, lower, unit requirement.

The available subsidy of \$1.2 million is sufficient to cover up to 8 units (5 1-bedrooms and 3 2-bedrooms).³ The Commissioner can grant this waiver without needing the approval of the Board of Estimates, provided that the units are provided at the income tiers required by Section 2B-21(b)(2)(i). In order to provide this waiver the PILOT would need to be increased to the legal maximum. If the PILOT is not increased, this waiver automatically eliminates the requirement to provide any inclusionary units, given that HCD does not have supplementary resources to contribute.

Thus, as none of the above three waiver modifications apply under these circumstances, the Inclusionary Housing law requires the Commissioner to exempt this project.

CONCLUSION

Based on the foregoing analysis, the Inclusionary Housing law requires that the Housing Commissioner must fully waive the Lexington Square project from mandatory compliance.

³ The method to determine "financial impact" is to calculate the present value of the total lost rent imposed by the IH requirement over the period of affordability required by the law. In Section 2B-51(a) the law requires a 30-year affordable rent for the units under the law. The calculation for that total impact assumes modest (3%) growth in the financial impact over the lifetime of the requirement and a discount rate for the present value of 6%. This methodology calculates the lifetime financial impact as described, but seeks the unit count for which \$1.2 million is the lifetime impact.

VOLUNTARY COMPLIANCE AGREEMENT

Despite the fact the Commissioner is required by the Inclusionary Housing law to exempt the Lexington Square project, HCD, BDC and the development team have been working to develop a program of voluntary compliance, in keeping with the spirit of the law.

The terms of this proposal are that the development team has agreed to voluntarily include twelve (12) units of affordable housing at the following rates:

Chart 2: Proposed Unit Counts for Affordable Units at Lexington Square

No. of units	Household income	Affordable housing cost
8 1-BR units	80% of Area Mean Income	Low
2 2-BR units	80% of Area Mean Income	Low
1 1-BR unit	60% of Area Mean Income	Very Low
1 2-BR unit	60% of Area Mean Income	Very Low
Total: 12 units		Total Cost: \$1,362,112

While the development team was aware that the remaining available public subsidy would provide enough money to add eight (8) units of affordable housing as discussed above, they, HCD and BDC all agree that, for this particular project, increasing the number of units by 50% more than the minimum to twelve (12) units represents a firm and fair commitment on the part of all parties in keeping with the spirit of the purpose of the Inclusionary Housing law for the citizens of Baltimore. Additionally, it is important to note that the twelve (12) units of affordable housing, which bear a cost of \$1,362,112, would be provided by the development team with no offset from any additional public subsidy.

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cc: Ms. Angela Gibson, *Mayor's Office of Government Relations*
 Ms. Kaliop Parthemos, *Deputy Mayor*

ATTACHMENT 'A'

FISCAL CALCULATION OF FULL COST

1) Unit Count

The Inclusionary Housing law would require that 59 units of the proposed 296 unit project (20%) be affordable, broken down as follows:

Chart 3: Unit Counts for Affordable Units at Lexington Square

% of IH Units	No. of units	Household income	Affordable housing cost ⁴
30%	18 units	30% of Area Mean Income	Extremely low
25%	15 units	60% of Area Mean Income	Very Low
25%	15 units	80% of Area Mean Income	Low
20%	11 units	80-120% of Area Mean Income	Moderate
Total	59 units		

The available affordable units must be equivalent in size to the market rate units. In other words, the number of one-bedroom affordable apartments must be proportionate to the number of one-bedroom market rate units in the project. Based upon of the number of one- and two-bedroom market rate units proposed by the developer for Lexington Square,⁵ HCD projects the number and size of the affordable units at each income tier as follows:

Chart 4: Affordable Units Count per Income Tier by Bedroom

Unit Size	30% AMI	60% AMI	80% AMI	100% AMI	Total
1-BR	12	10	10	8	40
2-BR	6	5	5	3	19
Total	18	15	15	11	59

2) Area Median Income and Maximum Rent

Area Median Income (“AMI”) for the Baltimore Metropolitan Statistical Area is a figure computed by HUD and used in all affordable housing programs, including Inclusionary Housing, to reflect regional income standards and to compute affordable costs and income limits. The income for a household of four at 100% of AMI in 2012 was \$85,600 per year. The following income limits apply to households in the Inclusionary Housing Program:

Chart 5: Household Maximum Incomes by Unit Size and Income Tier

Bedrooms	30% AMI	60% AMI	80% AMI	100% AMI
Studio	\$18,000	\$35,952	\$45,500	\$59,920
1-Bedroom	\$19,300	\$38,520	\$48,750	\$64,200
2-Bedroom	\$23,150	\$46,224	\$58,500	\$77,040

⁴ Article 13, § 2B-3(b) of the Baltimore City Code.

⁵ Based on *pro forma* submitted to HCD and developer communication that roughly 2/3 of the units are projected be 1-bedroom

The maximum housing cost under the IH law is described in Section 2B-3(b) as “not more than 1/12 of 30%” of the applicable income maximum. By applying that formula (Maximum Housing Cost = AMI limit for Unit/12 * 30%) we find the maximum rents for the units in this project as follows:

Chart 6: Maximum Housing Cost (Rent) per Unit Size per Income Tier

Unit Size	30% AMI	60% AMI	80% AMI	100%AMI
1-Bedroom	\$482.50	\$963.00	\$1,218.75	\$1,605.00
2-Bedroom	\$578.75	\$1,155.60	\$1,462.50	\$1,926.00

These figures represent the maximum rent that can be charged to a household occupying that unit under the rules of the Inclusionary Housing program, and define the level from which HCD calculates “financial impact” as described under the law.

3) Market Rate Rental Information and Financial Impact

Based on information presented by the Developer, and researched by HCD,⁶ HCD projects that market rate rents for this project will be no less than \$1,600 per one-bedroom and \$2,100 per two-bedroom unit per month. The definition of ‘housing cost’ under the Inclusionary Housing program does not include necessary utilities, or required expenses beyond rent [Section 2B-3(f)(2)].

The financial impact, or loss of rent per unit, is the market rent for a given unit less the affordable rent. Based on the projected market rents for the project and the maximum rents allowed by the Inclusionary Housing program from Chart 4, HCD projects that the financial impact per unit will be:

Chart 7: Financial Impact of Affordable Units Per Month by Bedroom Size and Income Tier

Unit Size	30% AMI	60% AMI	80% AMI	100%AMI
1-Bedroom	\$1,117.50	\$637.00	\$381.25	\$0
2-Bedroom	\$1,521.25	\$944.40	\$637.50	\$174.00

HCD previously developed a methodology for evaluating these monthly shortfalls under the requirement in Section 2B-4(f) that the inclusionary units “not impose additional finance burdens on a developer or a residential project...the intent of this subtitle is that the cost offsets and other incentives authorized under it will fully offset any financial impact resulting from the inclusionary requirements imposed.”

⁶ HCD staff called a number of comparable Westside and Downtown apartment complexes as well as Downtown Partnership of Baltimore to determine comparable rate information.

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The method to determine “financial impact” is to calculate the present value of the total lost rent imposed by the IH requirement over the period of affordability required by the law. In Section 2B-51(a) the law requires a 30-year affordable rent for the units under the law. The calculation for that total impact assumes modest (3%) growth in the financial impact over the lifetime of the requirement and a discount rate for the present value of 6%.⁷

The resulting calculation is that for every \$100 dollars of monthly financial impact the current value of the total financial impact is \$23,095. For the impacts set forth in Chart 5 the total lifetime impacts per unit type for Lexington Square are:

Chart 8: Total 30-year Financial Impact Per Affordable Unit by Type

Unit Size	30% AMI	60% AMI	80% AMI	100% AMI
1-Bedroom	\$258,092	\$147,118	\$88,052	\$0
2-Bedroom	\$351,340	\$218,114	\$147,234	\$40,186

4) Total Financial Impact

The total financial impact of compliance with the Inclusionary Housing law is the per-unit lifetime financial impact calculated in Chart 6 multiplied by the total number of units by type from Chart 2. The result of that calculation is:

Chart 9: Total Lifetime Cost per Affordable Unit Type Given Projected Unit Count

Unit Size	30% AMI	60% AMI	80% AMI	100%AMI	Total
1-Bedroom	\$3,019,677	\$1,434,403	\$858,502	\$0	\$5,312,582
2-Bedroom	\$2,129,121	\$1,101,474	\$743,530	\$162,352	\$4,136,477
Total	\$5,148,797	\$2,535,877	\$1,602,033	\$162,352	\$9,449,059

Thus, the total overall additional cost to the Lexington Square project imposed by the terms the Inclusionary Housing Law is \$9,449,059.

⁷ Growth assumption is based on trend of rental rate growth exceeding AMI growth in Baltimore, particularly for Downtown apartment complexes. Discount Rate is based on standard assumption in the City’s Finance Department, BDC and HCD projections.