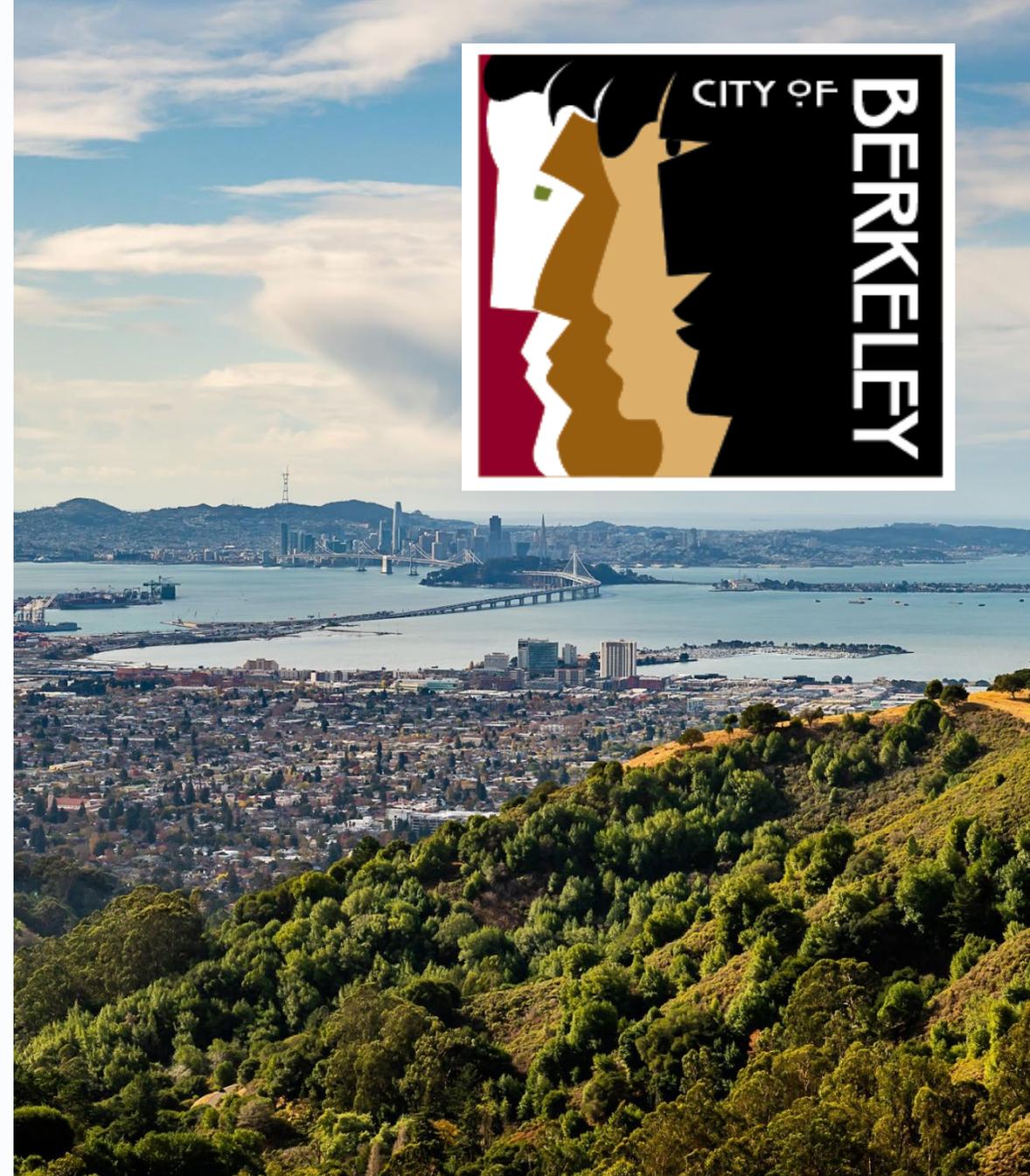
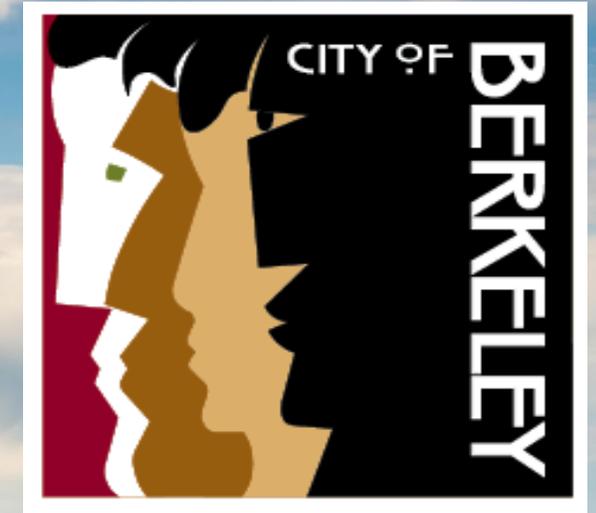


Residential Feasibility Analysis & In-Lieu Fee Recommendations

May 21, 2024

Health, Housing, & Community Services
Planning & Development

Strategic Economics
Street Level Advisors



Agenda

Introductions

Background

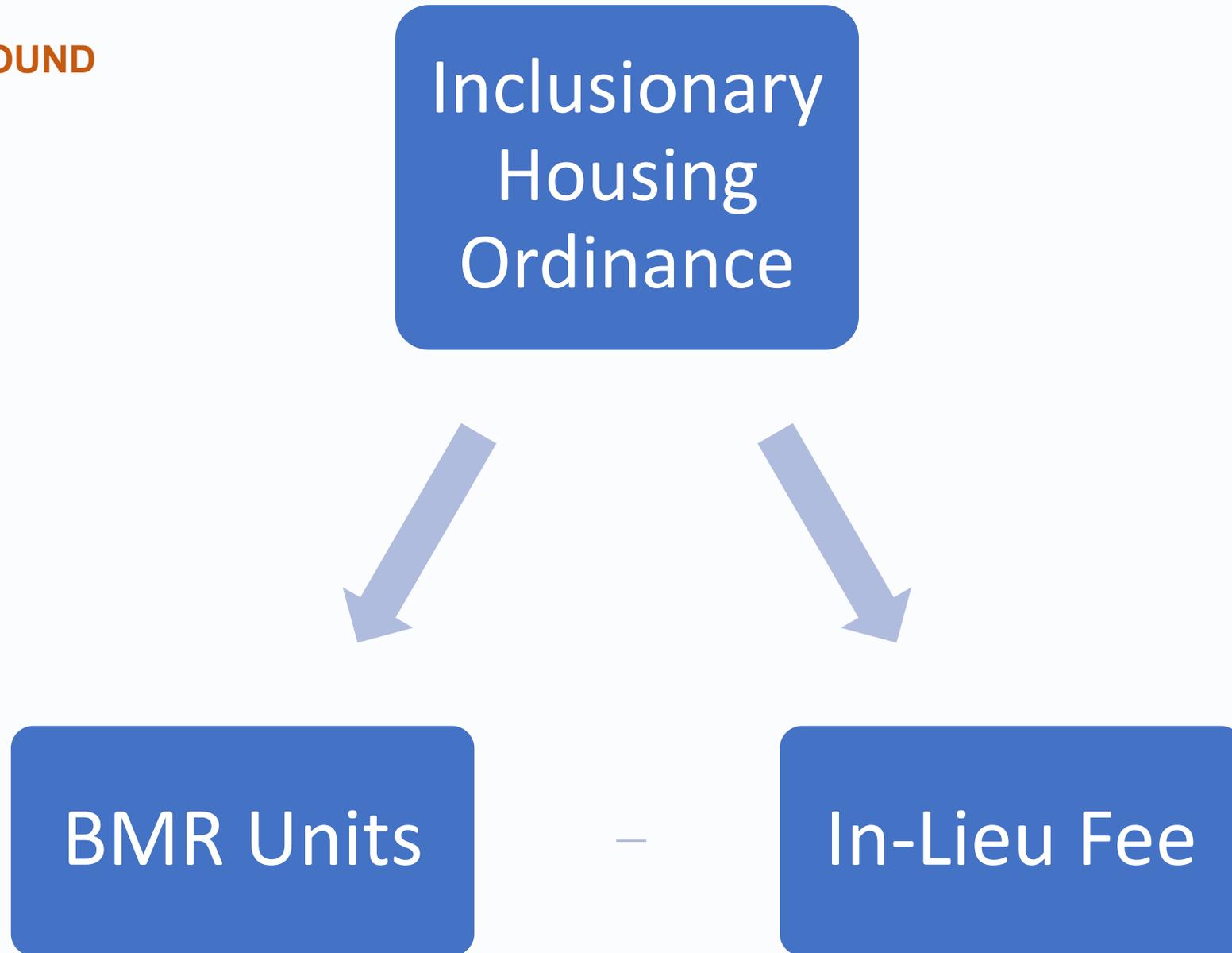
Goals

Findings & Recommendations

Next Steps

Questions

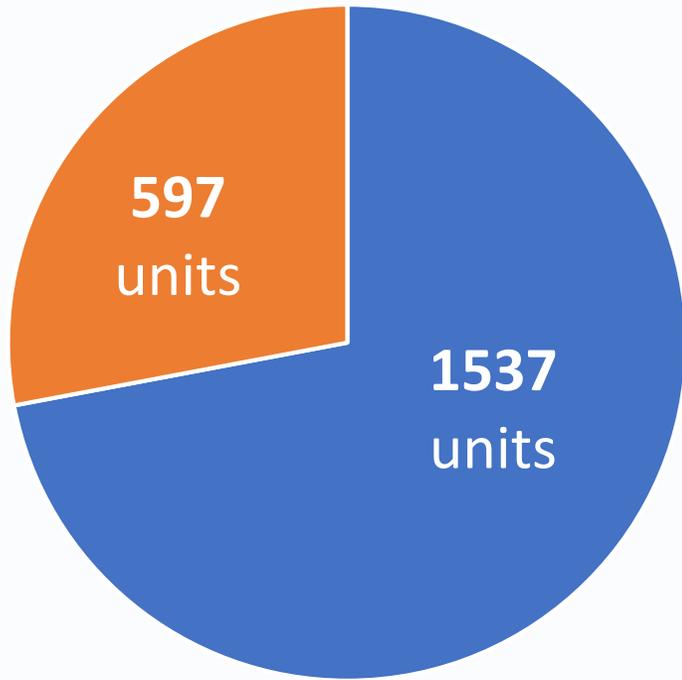
BACKGROUND



BACKGROUND

Berkeley's Affordable Housing Portfolio

Affordable Housing by Type



- Subsidized Units (HTF)
- Unsubsidized Units (BMR)

Housing Trust Fund Sources

- In-Lieu Fee
- Measure P
- Measure U1
- Measure O

BACKGROUND

IHO Revisions

- Feb 2023: Adoption of IHO & direction to conduct study
- Ownership and rental fees coordination
- Square footage In-Lieu Fee (RUFA)
- Covid/Inflation consideration
- Tiered fee + 5,000 sq ft exemption

BACKGROUND & REVIEW

Additional Housing Policies

HARD HATS

Prevailing Wage

Bird Safe

Purpose of Study

- **Analyze the In-Lieu Fee**
- **Analyze additional housing policies**
- **Recommend fee levels & policy options**

Policy Goals

Continue producing affordable housing

Support the financial feasibility of the housing market

Offer flexibility

Promote Middle Housing product types

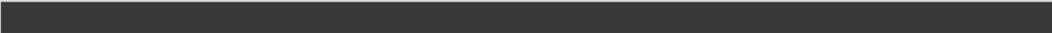
Work Session Goals

- **Review methodology, findings, and recommendations**
- **Answer your questions**
- **Receive input on recommendations for adoption**

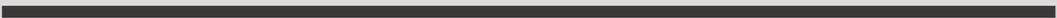


Berkeley City Council Work Session

May 21st, 2024



Methodology



We used three approaches to evaluate maximum reasonable in-lieu fee levels

Affordability Gap:

the capitalized difference in revenues between a market and BMR* unit

Production Cost Affordability Gap:

the difference between capitalized value of BMR unit revenue and the cost to produce a unit of income-restricted housing

Average Local Contribution:

the average City of Berkeley contribution to 100 percent affordable projects

*BMR = below market rate; i.e., a deed-restricted affordable housing unit

Peer city fee and policy comparisons provided regional context

- Provides regional context for affordable housing impact fees
- Gives insight as to how fees might influence where development takes place
- Berkeley has a relatively high inclusionary requirement
- Berkeley's housing market is unique

City	% On Site Affordable Units Required	In-lieu Fee*	Year Enacted
Berkeley	20%	\$56.25 per net residential square foot	2023
Alameda	15%	\$20,342 per unit	2023
Emeryville	20%	\$31,032 per unit	2023
Fremont	12.9% for rental projects	\$27.00 per residential square foot	2022
Hayward	6% for rental, 10% for ownership projects	\$19.37 per residential square foot	2017
Livermore	10% for projects downtown, 15% for projects elsewhere	\$29.23 per residential square foot	2023
Oakland	10% of project if providing low- or moderate-income units, or 5% if providing very low-income units	For multifamily projects: \$22,000 per unit in Zone 1 \$17,750 per unit in Zone 2 \$12,000 per unit in Zone 3	2023
Pleasanton	15%	\$45,083 per unit	2023
San Francisco	All requirements below temporarily reduced by 50%: 20% for small projects, 25% for large rental projects, 33% for large ownership projects	50% of \$199.50 per gross square foot	2019
San Jose	15%	Moderate Market Areas: \$18.26 per net residential square foot Strong Market Areas: \$43 per net residential square foot	2022/2023

*Note that the exact application of these fees varies from city to city. Examples of potential differences include application based on building area versus unit area, various exemptions, and potential differences within subareas of the cities.

Source: City Websites and Publications, 2024; Strategic Economics, 2024.

Prepared 7 development prototypes to test financial feasibility considerations

- Prototypes are hypothetical developments used to test financial feasibility
- Based on recent and proposed developments in Berkeley
- External sources informed Missing Middle prototypes
 - “Missing middle” refers solely to building type/density for this study’s purposes
- Prototypes vary by:
 - Height
 - Tenure
 - Density
 - Parking ratio/format
 - Use of State Density Bonus Law

Mid and high-rise prototypes

	4-Story GLA	6-Story Midrise	8-Story Midrise	18-Story High-rise
Example				
Description	Micro-studio units with shared common spaces	Podium style midrise	Podium style midrise	Type 1 high-rise
Floors	4	6	8	18
Housing Units	36	75	120	240
Density (unit/acre)	180	150	240	480
Tenure	Rental	Rental	Rental	Rental
Uses Density Bonus	Yes	Yes	Yes	Yes

Source: Strategic Economics, 2024.

Missing Middle prototypes

Small Lot Single Family

Fourplex/ Townhomes

10-Unit Small Multifamily*

Example



Description

Multiple single-family homes on a standard single family lot size

Stacked townhomes on a standard single family lot size

3-story multiplex with surface parking

Common Location

West Berkeley

West Berkeley

n/a

Floors

3

3

3

Housing Units

3

4

10

Density (units/acre)

30

40

50

Tenure

Rental & Owner

Rental & Owner

Rental & Owner

Uses Density Bonus

No

No

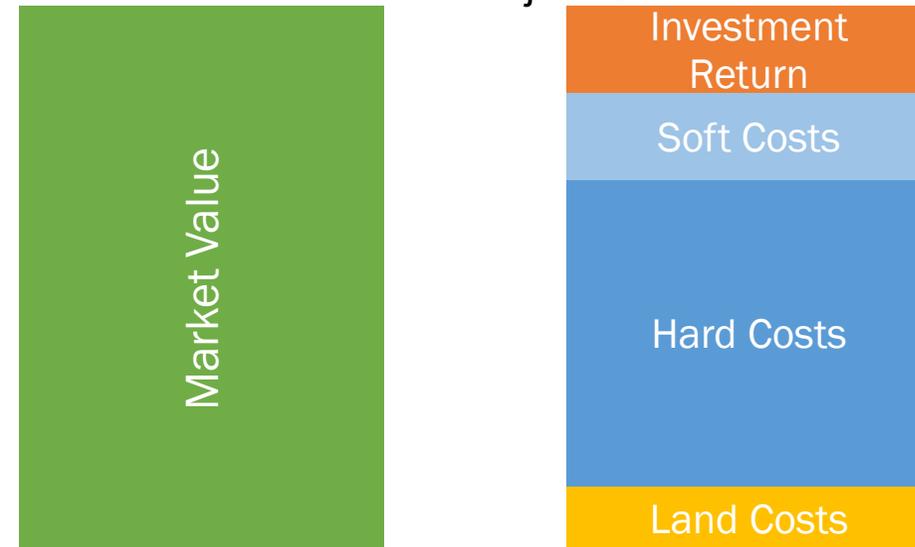
No

Note: This prototype draws from Opticos' Missing Middle design guidelines, since it is a development type not commonly seen in Berkeley.
Source: Strategic Economics, 2024.

The prototypes were tested in a financial feasibility analysis

- Determines if a project generates sufficient revenues to justify the costs and risks of building
- Represents perspective of a developer considering site acquisition and construction of a housing project

Components of Financial Feasibility: Project Value and Project Cost



Source: Strategic Economics, 2024.

There are two main metrics to measure return for housing development projects

Yield on Cost:

- The capitalized net operating income divided by the total cost to develop the property
- Used for rental projects
- 6% feasibility threshold

Return on Cost:

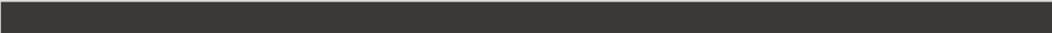
- The remaining revenue after subtracting total development costs, divided by the total cost of development
- Used for ownership projects
- 8% feasibility threshold

Feasibility results are a snapshot of current conditions; development conditions change

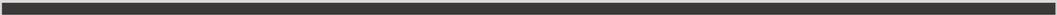
- All aspects of project costs, revenues, and required return change over time
- Most factors are outside the control of the City
- Feasibility analyses need to be conducted regularly

Cost and Revenue Change Impacts on the Return on Cost of One Ownership Unit						
		Change in Sales Value				
		-10%	-5%	0%	5%	10%
Change in Development Costs	-10%	29.16%	36.33%	43.51%	50.69%	57.86%
	-5%	22.36%	29.16%	35.96%	42.76%	49.55%
	0%	16.24%	22.70%	29.16%	35.62%	42.08%
	5%	10.71%	16.86%	23.01%	29.16%	35.31%
	10%	5.68%	11.55%	17.42%	23.29%	29.16%
	15%	1.08%	6.70%	12.31%	17.93%	23.54%

Source: Strategic Economics, 2024.

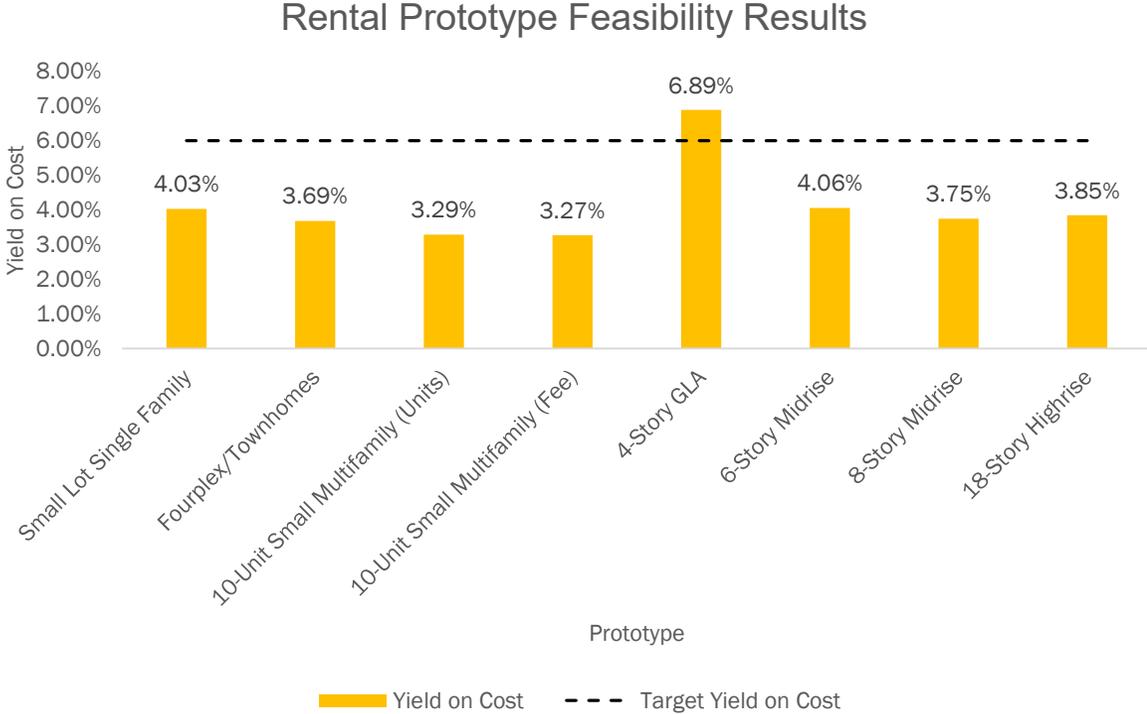


Findings



Current development conditions limit the rental prototypes' feasibility

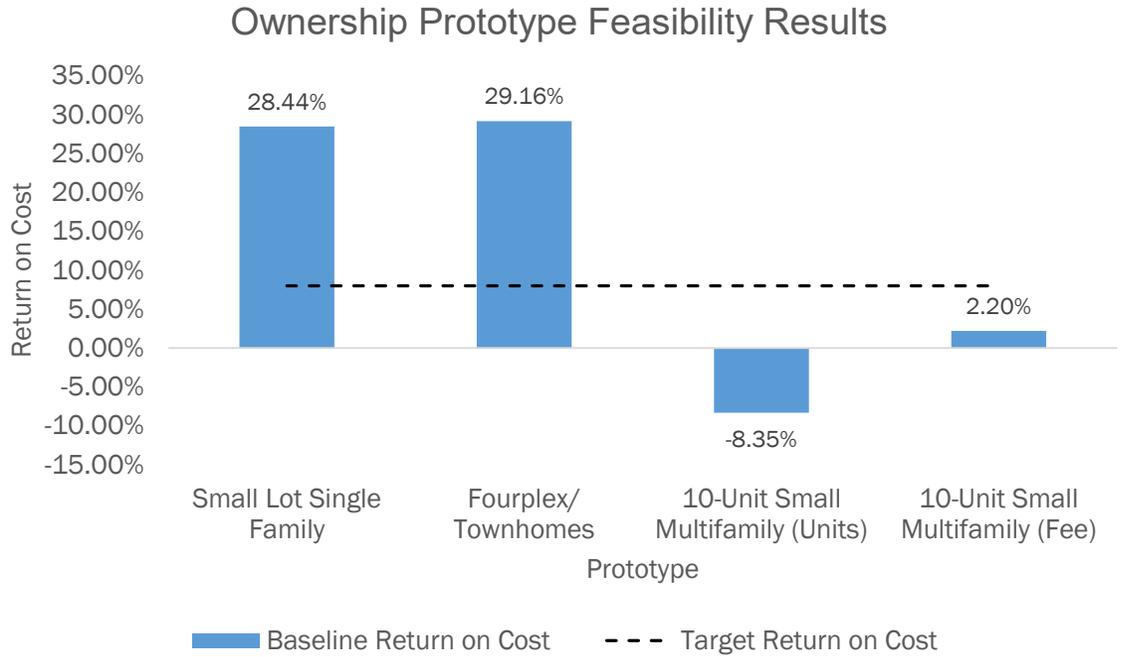
- Only the 4-Story GLA is feasible in current development conditions and under the current in-lieu fee



Source: Strategic Economics, 2024.

Some ownership Missing Middle products are currently feasible, but face other challenges

- Feasible:
 - Small Lot Single Family
 - Fourplex/Townhomes
- Feasibility supported by high sales prices as a luxury ownership product
 - BUT, challenged by limited site opportunities and pool of developers pursuing small projects
- Infeasible:
 - 10-Unit Small Multifamily



Source: Strategic Economics, 2024.

Maximum reasonable in-lieu fees range from \$59 to \$118 per square foot

- Affordability gap: comparable to cost of meeting inclusionary requirement
- Production cost affordability gap: cost gap to produce an affordable unit
- Local contribution: average City contribution to produce an affordable unit

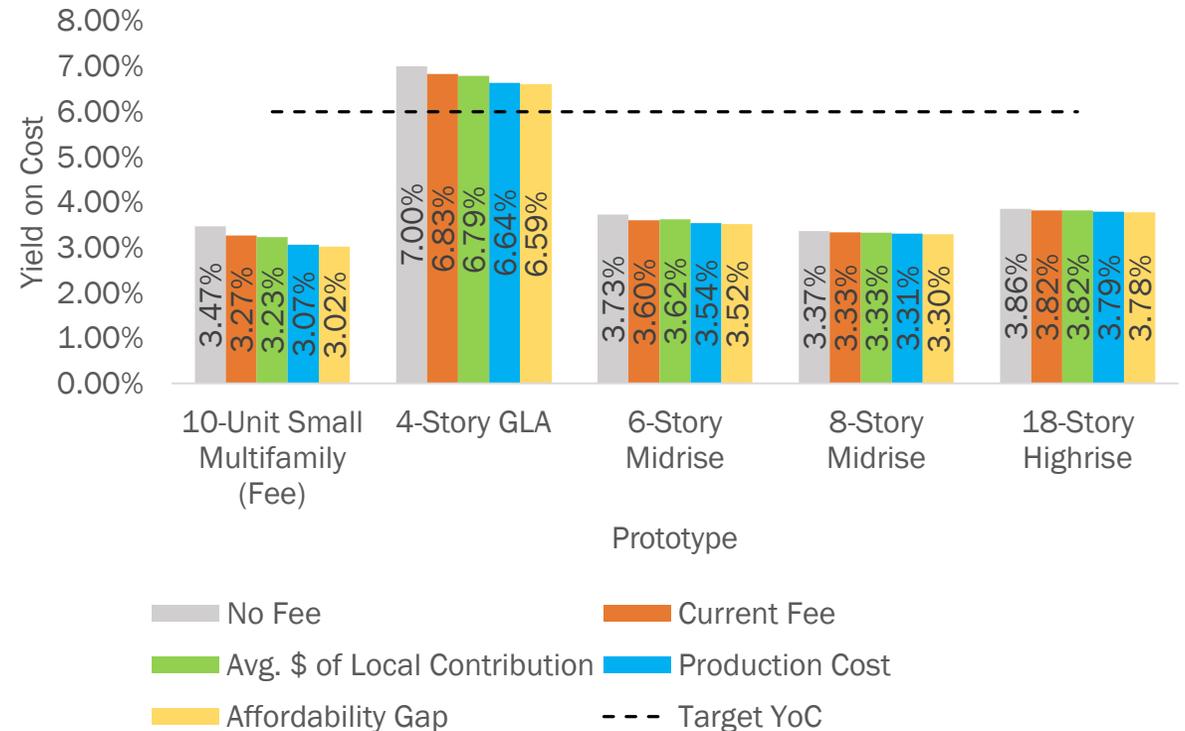
In Lieu Fee Results by Approach			
	Affordability Gap	Production Cost	Local Contribution
Average per Unit	\$388,374	\$342,432	\$193,348
Average per Square Foot of Market Rate Project RUFA	\$117.69	\$103.77	\$58.59

Source: Strategic Economics, 2024.

Market conditions limit feasibility for most residential prototypes, regardless of fee level

- All but the GLA prototype are infeasible even without the fee
- Infeasibility driven by elevated construction & financing costs and slower rent growth
- The impact of the in-lieu fee is low for Density Bonus projects
 - Fee is only charged to non-bonus square footage
 - Fee is prorated for remaining obligation above the mandatory on-site BMR units

In-Lieu Fee Analysis Sensitivity Results - Rental

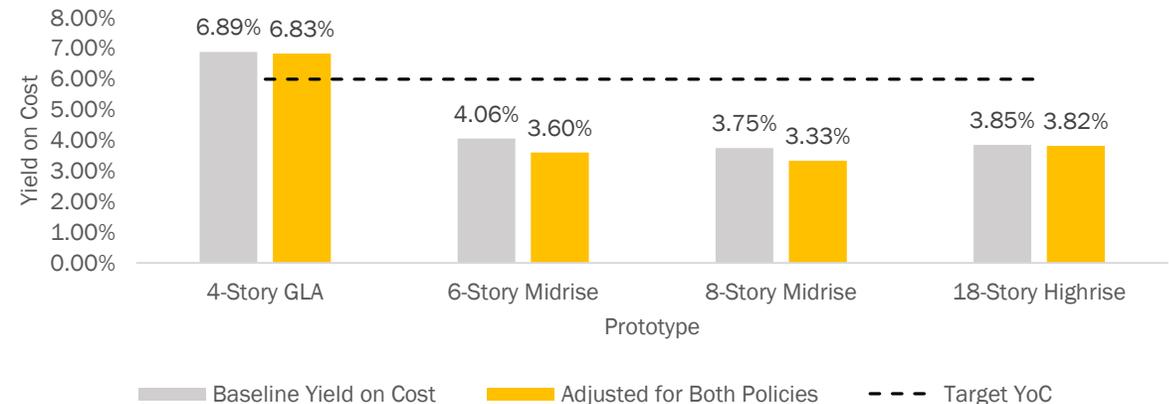


Source: Strategic Economics, 2024.

Labor and construction policies negatively impact feasibility

- Bird Safe Building requirements marginally reduces feasibility
 - 1% to 1.5% difference in hard costs (labor and materials)
- HARD HATS has similar impact to shift from non-union to union labor for midrise projects
 - 18% to 25% difference in hard costs
 - Cost increase is much less significant for high-rise projects
- Prevailing wage would be similar to union labor / HARD HATS

Financial Feasibility Impacts of HARD HATS and Bird Safe Building Requirements



Considerations for adjusting the in-lieu fee level / policy

- Most of the tested prototypes are currently infeasible
 - Most prototypes cannot support current in-lieu fees
 - BUT, in-lieu fees are not the primary driver of feasibility challenges
 - Some projects still developed due to unique circumstances
- In-lieu fees are a critical source of affordable housing funding
- Developments that pay the full fee—typically smaller and Missing Middle projects—are more sensitive to changes in fee level
- Most larger projects pay a prorated fee to satisfy remaining inclusionary requirements; these projects provide on-site BMR units to receive State Density Bonus

Recommendations

Apply the same in-lieu fee to all residential development projects

- Change the current exemption for projects under 5,000 square feet, to an exemption of the first 5,000 feet of *every* project that pays the full fee
- Eliminate the phased in fee for projects between 5,001-12,000 sf
- Apply the same in-lieu fee at the current maximum level (\$56.25) to all new residential developments

Exempt the first 5,000 sf of RUFA for projects paying full in lieu fee

- This exemption supports the production of Missing Middle housing, as these project types are less likely to be providing on-site units to gain access to the Density Bonus
- This reduces the fee per square foot of project area for these development types
- Projects that select mixed-compliance, would pay a residual fee based on the full RUFA (no exemption)

Maintain the existing \$56.25 maximum fee level as the universally applicable fee

- While the fee could justifiably be increased, maintaining the current maximum level supports the production of new housing by not increasing the fee when market conditions are challenging
- This fee level is approximately equivalent to the City's direct contributions to the cost of leveraging an off-site affordable housing unit
- Therefore, maintaining the fee at the current maximum allows the City to continue supporting off-site affordable developments

Continue to adjust the in-lieu fee based on the California Construction Cost Index

- Regular adjustment of the fee increases the likelihood that the revenue collected will continue to support a comparable number of affordable units in future 100 percent affordable housing projects.
- The in-lieu fee increases every two years since its last adoption in 2023; the next increase is proposed to still occur July 1, 2025

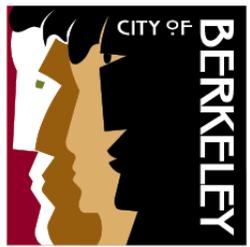
BACKGROUND & REVIEW

Next Steps

Questions

Housing Advisory/Planning Commission

Adopt Resolution/BMC Amendments



Questions

