MANNA, INC.

INCLUSIONARY ZONING OWNERSHIP:

LESSONS FOR THE DISTRICT FROM COMPARABLE CITIES

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Executive Summary

This report focuses on challenges with the ownership side of the District's Inclusionary Zoning (IZ) program, and lessons learned from cities with similar economic and housing conditions. The District has the opportunity to learn from past mistakes, to pull best lessons from these cities, and to be the first high-priced market to deal with rising fees facing lower income buyers. As these cities' policies will reveal, the District needs to inject flexibility into its program in order to robustly contribute to the creation of new ownership units and benefit lower income individuals and families in the District of Columbia.

Permanent Resale Restrictions

From the beginning, IZ ownership, specifically permanent resale restrictions, has been controversial in the District (see a brief history in Appendix I). Opponents to permanent resale restrictions were concerned about the effect on the economic advancement of lower income households. In essence, they believed that the design of IZ ownership units took away the only substantial asset many lower income families have, making the units more akin to rental or limited equity cooperatives.

Issues with Predecessor to IZ Ownership

Similar to IZ ownership units are Affordable Dwelling Units (ADUs) that were integrated into market-rate condo buildings across the city in the 2000s. Issues faced by owners of these units include:

- escalating condo fees, some increasing over 100%
- expensive special assessments
- being outnumbered and outvoted in their condo associations
- sub-par and expired materials, including flooring and appliances
- structural issues, such as cracks in the walls and damaged plumbing
- difficulty refinancing
- inability to sell units to buyers using FHA loans
- gaining permission to rent, but at a rate that does not cover monthly costs

Lessons Learned From Similar Cities

The structure of the District's IZ program is often compared to Montgomery County's program. Such comparisons are inappropriate as the District's economy, housing market, size of IZ units, available land, and population are different The most comparable cities to the District are San Jose, San Francisco, and Boston. Helpful lessons from each city include:

San Jose
Instead of permanent restrictions, San Jose employs a **recapture model** that recaptures "subsidy" in the unit upon resale but gives the owner access to any equity appreciation. This model helps **maintain homeownership as an asset** for households that purchase. It also allows owners to **easily sell in the case of rising condo fees** they cannot afford.

San Francisco
Over time, San Francisco has adopted an **in-lieu fee system**, which generates funding for off-site ownership development instead of IZ unit creation within market-rate buildings. Though not San Francisco's expressed purpose, this kind of system **allows the creation of larger units for families** as well as a way to **avoid quickly escalating condo fees**, which is a serious issue in San Francisco. Boston has a similar in-lieu system, with even higher fee amounts.

Boston
Boston's program highlights **flexibility**, both in regards to development and resale. If the allowed increases push an owner's resale price beyond what is affordable to targeted income levels, the Boston government will either 1) purchase the unit and sell at a lower price; 2) permit a higher income buyer to purchase the unit; or 3) give downpayment assistance to the next buyer. Massachusetts has also attempted to pass legislation **capping condo fee increases for IZ owners living in market-rate buildings.**

Ultimately, the recommendations of this paper are made with flexibility and success in mind, for both the owners and the District government. Without change, the following three things are in jeopardy: 1) the financial well-being and economic advancement of lower-income households; 2) the administrative capacity and costs for DHCD; and 3) successfully meeting affordable housing development goals. The District has a golden opportunity to make the ownership side of Inclusionary Zoning not only work, but excel.

Inclusionary Zoning Ownership in DC

As laid out in the 2012 Comprehensive Housing Strategy Task Force Report, the District government aims to create 10,000 new affordable housing units by 2020.[1] With this goal in mind, the report lays out several housing financing and production tools, and calls for the study of existing tools to ensure they are operating efficiently and producing positive outcomes. One of the tools identified for study is the District's Inclusionary Zoning (IZ) program, and this research specifically focuses on IZ ownership units.

Inclusionary Zoning is an affordable housing policy that links the production of affordable housing to the production of market-rate housing, and was introduced in the District of Columbia through legislation in 2006.[2] The District's IZ program requires an 8-10% unit set-aside in new rental or condominium developments of 10 or more units, and in existing buildings expanding by 50% or more. Developers receive bonus density in exchange for the creation of IZ units, and may opt for other incentives. Renters and buyers of these units must be under 80% of the Area Median Income (AMI), which is $86,000 for a family of four. The Office of Planning monitors developer compliance with IZ regulations, while the Department of Housing and Community Development (DHCD) administers the program for buyers and renters. According to the latest report on the program,[3] 18 units have been produced with the following breakdown -17 units for 80% AMI and 1 for 50% AMI; 15 rental units and 3 ownership units. As of July 2013, 14 units were rented and one sold.[4] The pipeline of IZ applicable projects is reported at 104, totaling 1,079 units. As in past reports, there is no breakdown of rental and ownership units in the pipeline.

IZ ownership units are permanently restricted, requiring all owners to sell to buyers in their same income category for the life of the unit and using a maximum resale formula to determine sales price.[5] Rental of these units is not allowed unless owners receive special exemptions, and the maximum rental price and income of the renter is determined by the Department of Housing and Community Development (DHCD). At the time of sale, purchasers can spend no more than 41% of their income on the unit, including mortgage principal, interest, taxes and insurance. DHCD encourages developers to use a par value system to set initial condo fees, but the rate of future increases and distribution of special assessment costs are left to the condo association.

Both available public information on, and the practical aspects of, purchasing/selling IZ ownership units have left buyers and developers in the dark. In regards to public information, DHCD fails to mention the permanent restrictions tied to IZ ownership units in both their mandatory training for IZ lottery applicants and on their website. This omission is problematic as it leads applicants to believe that these are regular ownership units. Another issue was a clause in the IZ ownership units' covenants that FHA will not accept. Potential buyers of these units, due to their incomes, are more likely to use FHA loans. Lack of access to these loans contributed to units remaining on the market for over 18 months. One developer even sued the District after not being able to sell the only two IZ units in his development.[6] The District has recently amended this clause.

Challenges in Predecessor to IZ Ownership

Some of the issues faced in the Affordable Dwelling Units (ADU) program highlight problems that could take place in the District's IZ program, causing financial issues for owners and administrative nightmares for DHCD. Per land agreements between the District government and developers in the 2000s, ADUs were created in market-rate condo buildings. The ADUs in these buildings comprise 5-20% of the total units, and each has 20-year resale/rental restrictions.[7] Manna is aware of 9 of these buildings with approximately 170 studio, one-bedroom and two-bedroom ADUs, though there may be more. Issues faced by these owners have included:

- escalating condo fees, some increasing over 100% (See Figure 1 below)
- expensive special assessments (most recent - $1,000 legal fee at Chase Point)
- being outnumbered and outvoted in their condo associations
- sub-par and expired materials, including flooring and appliances
- structural issues, such as cracks in the walls and damaged plumbing
- difficulty refinancing
- inability to sell units to buyers using FHA loans (DHCD plans to ammend each of these covenants)
- inability to sell parking units purchased as a part of their original purchase contract (DHCD requires them to be sold separately)
- gaining permission to rent, but at a rate that does not cover monthly costs

Figure 1 - ADU Condo Fee Increases by Building

Condo Project	Location	Original Condo Fees for ADU	Current Condo Fees for ADU	Change
Chase Point	Friendship Heights	$324.00	$700.00	116%
Fedora	Columbia Heights	$166.00	$351.00	111%
Barcelona	Columbia Heights	$169.00	$350.00	107%
Kenyon Square	Columbia Heights	$280.00	$520.16	83%
Verona Parc	Columbia Heights	$214.35	$354.00	65%
Union Row	Columbia Heights	$375.00	$485.00	29%
City Vista K and L Buildings	Mount Vernon	$343.00	$378.29	10%
Note: This data was collected from a sample of ADU owners in early 2012. Original condo fees are from when owners moved in, which was from 2006-2007.				

Essentially, many of these owners have been priced out of their units, causing people to rent out illegally, borrow money from family and friends, take on two or three jobs, etc. Others are experiencing growing families, but are worried about selling their units due to 1) not being able to find a buyer in their income category because condo fees have risen so high, 2) not being able to make enough on the sale to move to a larger place due to capped maximum resale prices and the amount of structural and maintenance work required to get the unit ready for sale (as condo fees and special assessments have eaten up their reserves), 3) inability to use another Home Purchase Assistance Program loan, making it unlikely they will be able to purchase another place. Finally, there are others who would like to rent out legally for a short period of time and at a price that covers their monthly expenses, but it has been uncertain what DHCD will allow and how long the process will take.

As of June 4, 2013, after the passage of emergency legislation, months of in-depth meetings and intense bureaucratic work, DHCD has offered a process through which some of these ADU owners can sell or rent their units to buyers in higher income categories. ADU units are tied to certain income categories, and DHCD will determine if buyers in those income categories can afford the unit with the current condo fee. Owners required to sell to buyers under 80% AMI will sell at the same maxiumum resale price. If DHCD deems the unit unaffordable for someone under 80% AMI, then the current owner will be allowed to sell at market, sharing the appreciation with DHCD. DHCD is considering adding a flat rate for extraordinary expenses for owners required to sell to buyers under 80% AMI, as well as a small rental reserve for those who choose to rent their units for a period of time.

While there is a process for selling and renting, there is no solution allowing priced-out ADU owners to remain in their units. This has been especially difficult for owners approaching retirement and for others who hoped to, post the 20-year restriction, pass along their unit and the equity in it to their children. In order to build a better IZ program in the District, the failure of these ADUs and the hardships/experiences of these owners must be taken into account.

Inclusionary Zoning in Comparable Cities

The structure of the District's IZ program is often compared to Montgomery County's program. Such comparisons are inappropriate as the District's economy, housing market, available land and population are different, as well as the larger size of on-site units being created through the County's program. To make a more accurate comparison, this research uses population and Cost of Living Adjustment (COLA)[8], identifying cities that are within 10 percent variance of the COLA and within 350,000 (+) difference of the District's population of 601,723.[9] As exhibited in Figure 2 below, three cities are comparable to the District - San Jose, San Francisco and Boston.

Figure 2 - Cities by Population and Cost of Living Adjustment

City Name	State	2010 Census Total Population	Cost of Living Adjustment (%)
San Jose	California	945,942	3.3
Jacksonville	Florida	821,784	-35.7
San Francisco	California	805,235	9.3
Austin	Texas	790,390	-36.8
Columbus	Ohio	787,033	-38.2
Fort Worth	Texas	741,206	-36.9
Charlotte	North Carolina	731,424	-37.3
Detroit	Michigan	713,777	- 35.3
El Paso	Texas	649,121	-37.9
Memphis	Tennessee	646,889	-43.1
Baltimore	Maryland	620,961	-20
Boston	Massachusetts	617,594	-7
Seattle	Washington	608,660	-21.9

Each of these cities has similar housing goals to the District as it pertains to housing stock creation and affordable housing need. The following section will detail these cities' goals as well as their respective IZ policies, challenges and adaptations.

San Jose

As part of Santa Clara County, San Jose's Area Median Income for a family of four is $105,000. In California, each jurisdiction participates in developing 7.5-year housing production goals, known as Regional Housing Need Allocation (RHNA).[10] For 2007-2014, San Jose's share is 34,721 new housing units: 13,073 units for low, very-low, and extremely-low income households and 6,198 units for moderate-income households. As of December 2012, San Jose had reached 64% of its above moderate-income allocation, but only 13% for the remaining income levels (see Figure 3 below).

Figure 3: San Jose 2007-2004 Housing Production Goals[11]

Income Category	**Income Range**	**Number of Units**	**Total Units as of Dec 2011**
Above Moderate (Above MOD)	Above 120% AMI	12,315	7,826
Moderate (MOD)	81% - 120% AMI	6,754	928
Low (LI)	51% - 80% AMI	5,535	736
Very Low (VLI)	0% - 50% AMI	6,589	2,836
Total		31,193	12,326

The city reports decreased public funding amidst increasing market prices as impeding their ability to keep up with housing allocations for lower income households. In addition, San Jose identifies issues with its Inclusionary Housing program as contributing to the shortfall.

Currently, San Jose has an Inclusionary Housing policy in certain Redevelopment Areas across the city.[12] In 2010, the city adopted a citywide IZ ordinance for 20 + unit buildings, which has been legally disputed by a few developers ever since.[13] The Santa Clara County Superior Court officially struck down the ordinance on July 11, 2012. Legal challenges and market conditions have slowed down the entire IZ program, contributing to the creation of less affordable units. However, the case has been appealed and restructured, and the San Jose government estimates that the citywide policy will become operative in the next two years or more. To date, approximately 200 IZ ownership units have been created.

San Jose's IZ ordinance (both its current and future citywide program) requires a 15% set-aside of units in new residential developments; 6% available for 50% AMI and the other 9% for 80 and 120% AMI. If a developer chooses to set-aside 20% of the total units, they can create a mixture of 80 and 120% AMI units. Developers can also opt to pay in-lieu fees instead of providing units within the market-rate building. In calculating these fees, a 20% inclusionary obligation is used as opposed to 15%; the fees are also based on product type and the total average net living area of the units in the project, with maximums of $90,000 per condo unit and $120,000 per townhouse.[14] Using the same 20% requirement, developers can also opt to combine in-lieu fees with the provision of on-site or off-site affordable units. San Jose has not collected many fees in the last 10 years, but expects at least $3 million dollars in the next couple of years.

Specific to IZ ownership units, San Jose has a subsidy recapture program. IZ owners do not face resale restrictions and thus can sell their units at market rate. Upon the sale of the unit, an owner will pay back the difference between the original contract sales price and the appraised value at the time he/she purchased; any equity appreciation goes to the owner. For example, a moderate-income buyer purchases a unit for $230,000 that is worth $430,000. The $200,000 "subsidy" is recorded as a deferred soft second on the property. When the owner sells 10 years later, the unit sells for $530,000; the owner pays the $200,000 "subsidy" to the city and retains the $100,000 appreciation of the unit, minus any costs associated with the sale. Owners can also choose to sell to another buyer in a similar income category as long as the subsequent owner agrees to assume the $200,000 soft second. San Jose uses any recaptured funds for the perpetuation of other affordable housing programs.

There are few administrative costs associated with the ownership side of San Jose's IZ program, with administrators mostly focused on verifying applicants' incomes when units are first sold.[15] In regard to condo fees on IZ ownership units, San Jose does not have a way to control the rate of increases. The Housing Department is not aware of issues with escalating condo fees for their owners. However, the Department noted they may not have been notified as an owner can easily sell their unit if it becomes financially burdensome.

San Francisco

Similar to San Jose, California state law is instrumental in the development of San Francisco's affordable housing policies and goals. San Francisco's housing production goals for 2007-2014 totaled 31,193 new units (see Figure 4 below).[16] At the time of the last available update in December 2011, San Francisco had met 63.5% of the above moderate-income production goal and 37% of affordable housing goals (0-120% AMI). San Francisco's Area Median Income for a family of four is $101,200.

Figure 4: San Francisco County 2007-2014 Housing Production Goals[17]

Income Category	Income Range	Number of Units	Total Units as of Dec 2012
Above Moderate (Above MOD)	Above 120% AMI	15,450	9862
Moderate (MOD)	81% - 120% AMI	6,198	144
Low (LI)	51% - 80% AMI	5,322	782
Very Low (VLI)	31% - 50% AMI	3,875	987
Extremely Low (ELI)	< 30% of AMI	3,876	549
Total		34,721	12,324

The Planning Department reported another 5,600 units in the pipeline through 2016, with a fifth of those for moderate income households and below. The cost of development is extremely high in San Francisco, with a reported subsidy of $170,000 to $200,000 per unit for low and very low income households.[18] To actually meet 2007-2014 housing goals, over $2 billion is needed.

As part of meeting its affordable housing goals, San Francisco's city-wide Inclusionary Housing program creates what the city calls Below Market Rate units (BMRs) in developments of 10 + units. Depending on where developers build, anywhere from a 12-22% set-aside of BMR units is required.[19] If a developer chooses to develop off-site, they must do so within one mile of the original site and have a higher set-aside requirement. San Francisco's program has gone through many adaptions, including the option of in-lieu fees starting in 2002. These fees are much higher than San Jose, and are set solely by bedroom count - Studio=$179,952; 1 bedroom=$248,210; 2 bedroom= $334,478; 3 bedroom=$374,712. $17 million in-lieu fees were collected as of 2008.[20]

One issue that San Francisco has faced is shoddy construction in off-site buildings.[21] There have been an instance or two of developers subcontracting out to another developer, and not paying attention to construction quality. The Office of Housing sees this as an oversight issue that can be remedied by more closely inspecting off-site developments.

BMR ownership units are permanently restricted, which the Office of Housing makes extremely clear on their website and all other documentation. Maximum resale formulas include 5% for use of a realtor and the inclusion of up to $2,000 of any special assessments paid by the owner. The targeted household income levels differ depending on location. On-site ownership units sell at 90% AMI while off-site units target households at 70% AMI. In the Eastern Neighborhoods, units sell at 120-150% AMI, and a recapture method is used, providing a certain amount of equity to the owner depending on how long they have lived in the unit.

Rising condo fees have been a concern of various BMR owners.[22] In the last couple years, the Office of Housing has received a number of calls and inquiries from owners about assistance for increasing fees and being outvoted by their market-rate neighbors.[23] In addition to encouraging BMR owners to stay or serve on their condo boards, the Office has also considered funding to assist with fee increases. They first considered providing down-payment assistance funds, but were unable to do so due to stipulations tied to that funding source. Another idea for relief has been the establishment of a condo fee/special assessment loan fund in connection with San Francisco's new Housing Trust Fund. However, the Office of Housing has not been able to figure out underwriting for the fund or what amounts it would offer owners; the Office is also concerned about setting up such of fund due to the long-term funding implications.

It is possible that rising condo fees may affect an owner being able to sell to someone else in their income category. As such, the Office of Housing offers the same options devised for owners who have been unable to find a buyer for six months. Some of options include: (1) renting out for a year; (2) selling to someone who is not a first-time homebuyer; and (3) obtaining a waiver to exceed AMI category by 20%, but never above 120% AMI. To date, the Office of Housing has not seen a housing-to-income ratio that necessitated resale to someone above 120% AMI.

Boston

Earlier this year, Mayor Thomas M. Menino of Boston announced a plan to produce 30,000 new housing units by 2020.[24] Currently, an advisory panel of ten housing experts is meeting to create a comprehensive plan focused on market-rate and affordable housing production and preservation, as well as the needed financial leveraging tools. The Boston government reports that the previous housing strategy inaugurated in 2000, entitled *Leading the Way,* had created 20,473 housing units and invested more than $8 billion into the local economy.[25] Of those new units, 6,377 were affordable and another 12,611 affordable units were preserved. Affordable housing programs target families making under Boston's Area Median Income, which stands at $94,400 for a family of four.

Boston implemented its Inclusionary Development Program in 2000.[26] As with the other two cities, the policy has gone through several revisions. Currently, the Boston Redevelopment Agency (BRA) requires new residential developments of 10 + units to set aside 15% of the total units as affordable. Since 2006, developers have had the option of providing units off-site or paying in-lieu fees, though the BRA still has the authority to approve these options or not. In both cases, the set aside remains at 15%. Developers pay the higher of $200,000 per unit or half the difference between market and affordable unit prices; by mid-2008, the BRA had collected $19.5 million in fees.

The number of IZ ownership units in a building are split evenly between 80% AMI and 100% AMI. Units have 30 year resale restrictions, with a subsequent 20-year extension. The maximum resale price assumes an increase of 5% per year of the initial sales price, as well as realtor and sales fees. If these increases to the resale price go beyond what is affordable to the targeted income levels, the BRA has three options: 1) purchase the unit and sell at a lower price; 2) permit a higher income buyer to purchase the unit; or 3) give downpayment assistance to the next buyer. A reserve fund exists for the BRA to buy back units; part of this fund comes from in-lieu fees.

The 2006 policy changes were made in order to locate IZ owners closer to neighborhood services and build larger units for families.[27] At the time, a lot of high-cost, luxury building development was happening in downtown areas. The BRA was worried about location, IZ owners getting priced out of their units, as well as the smaller unit sizes. In-lieu fees and off-site construction allowed them to cater to families and build in areas of the city more conducive to long-term residency. Some of the in-lieu payments from the downtown area have amounted to $500,000 per unit or more, producing much more housing in other areas of the city.

Condo fee increases have also affected IZ owners in Boston. It is unclear how the BRA has dealt with this issue. There was a fund created for IZ owners in one specific building, but that lasted for only a year.[28] In Massachusetts, voting power on a condo board is the same proportion as an owner's condo fees.[29] If fees are much lower for an IZ owner, then he/she will have a lesser percentage vote. It has also been common for market owners to develop bitterness toward their IZ neighbors for having to subsidize them. This became a major issue in 2010, leading to a decision to set initial condo fees by floor area instead of contract sales price. In 2011, an amendment was referred to Massachusett's Joint Committee on Housing that called for a 3% annual increase cap on condo fees for IZ units.[30] In addition, it stipulated that affordable owners would not be required to pay for nonessential amenities. The amendment was studied and referred favorably to the Committee on House Rules, but no further action has been taken.

Recommendations

The below recommendations for the District's IZ program are based on the experiences of San Jose, San Francisco, and Boston, as well as past development experiences in the District and challenges in the District's ADU program. All of these recommendations are specific to the ownership side of the program only, and are geared toward creating a program that actually benefits owners and robustly contributes to ownership production in the city. While some recommendations can be enacted immediately, others will require changes by the Office of Planning and the Zoning Commission, or perhaps the City Council.

Full Disclosure

As mentioned earlier, the District does not currently publicly disclose the permanent resale/rental restrictions attached to IZ ownership units. Throughout the entire 2-hour training required for those wanting to enter the IZ lottery, restrictions are neither referenced in the power point presentation prepared by DHCD nor by the instructors. Language on restrictions is also absent from DHCD's IZ portion of their website. All of the other cities covered in this paper disclose the restrictions attached to their units, and San Francisco is particularly thorough, including a maximum resale formula calculator on their Inclusionary Housing webpage. The District should ensure full disclosure of IZ units' permanent resale restrictions in all DHCD-sponsored events and publications. Failure to do so will lead interested buyers to believe they are purchasing traditional ownership units with access to equity appreciation, the ability to take out an equity loan, and the freedom to rent per the rules of their condo association.

In-lieu Fees and Off-site Construction

In the interest of creating larger units for families and economically-viable living situations, we believe the District should consider both in-lieu fees and off-site construction. With onsite construction, unit sizes are determined by the make-up of market-rate units in a given development, and are typically studios, one-bedrooms and a fewer number of two-bedroom units. If the District wants to provide longer term ownership opportunities for families or individuals/couples planning to have children, then it should consider available avenues to build larger units. Also, in instances of high-priced condo buildings, IZ owners are less likely to be priced out by rising fees if their units are built in majority or all-affordable buildings. The current system lends itself to IZ owners being outvoted on condo boards and feeling sidelined or ostracized within their buildings.

As written in a recent national report on the state of Inclusionary Zoning by the Center for Housing Policy, "by working in partnership with affordable housing developers, in-lieu revenues can be combined with other public funds" to address various housing needs.[31] Fortunately, the District has many competent non-profit and for-profit developers that can adeptly make use of in-lieu fees or subcontract for off-site affordable ownership production. In fact, the District has successfully used in-lieu fees generated from downtown development in the past, partnering in the 1980s with developers like Manna and Jubilee Housing to develop 60 ownership units in Shaw and 60 rental units in Columbia Heights. We suggest the District consult affordable developers, as well the previously mentioned cities to determine the appropriate in-lieu fee structure for the District. In order to avoid issues faced by current ADU owners and San Francisco, construction quality should be monitored on any IZ unit, no matter where it is produced.

Recapture and Recycle

San Jose's subsidy recapture program was designed with economic advancement and minimal administrative costs in mind. The city wanted to ensure both a funding source for its affordable housing programs as well as the ability for IZ owners to have access to the appreciation of their homes and more easily move into the open market if they need to sell. For lower-income, first-time homebuyers, ownership property is often their largest and most important asset. The District's policy of permanent resale restrictions maintain the responsibility and financial challenges of homeownership for IZ owners, but eliminate any return on investment related to property, neighborhood and general real estate price improvements. Though this paper is not promoting this model, permanently restricted ownership units are better suited for those in higher-income categories with access to wealth through their families (who often own unrestricted property) or through their educational/job opportunities.

The District should consider both San Jose's recapture model as well as the recapture model detailed in draft legislation for the Housing Production Trust Fund, which responds to economic differences across the city (see Appendix I). Another consideration is recapturing the "subsidy" within the unit itself, keeping the unit affordable to different income categories for a longer period of time. In this scenario, the IZ owner will sell the unit at the market price, with the AMI of the buyer capped by a formula managed by DHCD. The assumed subordinate loan/subsidy will provide down payment funding and lowers the cost to the new buyer. The original buyer only receives gains based on increases in property value. The below examples are based on an 80% AMI unit sold at $200,000 but with an original market value of $400,000. Market Increase refers to potential appreciation on the market, the AMI increase is set at 3%, while the other columns refer to the maximum AMI category that could afford to purchase the unit after 5, 10 or 15 years.

Figure 5: In-Unit Subsidy Recapture and Resale

Market Incr.	AMI Incr.	5yr AMI	10yr AMI	15yr AMI
3%	3%	80%	80%	100%
5%	3%	100%	100%	120%
7%	3%	100%	140%	160%

Condo Fee Structure

As exhibited in the District, San Francisco and Boston, rising condo fees threaten to and have economically forced out ADU and IZ owners. Even though San Jose's recapture model allows owners to easily sell if fees rise beyond their ability to pay, this is not a viable, long-term policy. People become owners in order to avoid ever-increasing rents, benefit from stable mortgage payments, and to have a say in the common fees they will pay in their buildings. Condo fees are the only uncapped housing expense for IZ buyers, who get fixed rate loans and have real estate taxes capped by the District. These fees represent a much larger percentage of the housing payment for IZ buyers than market buyers. Why should the District and other jurisdictions continue to create and monitor ownership opportunities that price out low and moderate-income owners? Even if these owners are still able to find a buyer in their income category to sell to, why should the District support a policy that forces even a working person out of their home?

When it comes to on-site IZ units, the District needs to cap or somehow reduce the potential increases of condominium fees. Condo documents for mixed-income buildings should impose a 'par value system', where original fees are set based on relative prices and increased on the same annual percentage as all other fees. Alternatively, condo fee increases in IZ units could be capped at the inflation rate. The differentiation of condo fees for IZ owners institutionalizes a subsidy by other owners in the building, whose condominium fee increases will have to cover more than their square footage share of the expense.

This system comes with its own challenges. San Francisco's Office of Housing reacted to the idea with fear that it would cause even more bitterness from market rate owners, creating hostile living environments for IZ owners as took place in Massachusetts. In order for such a system to work in the District, it would have to be fully disclosed to each buyer before they purchase. The District should consult with Massachusetts law makers regarding the 2010 bill that proposed capped condo fee increases to see if there are any helpful lessons learned. Without some sort of condo fee structure for on-site units, IZ owners risk being priced out and the District risks increased administrative costs and challenges.

Flexibility, leading to Success

All of these recommendations are made with flexibility in mind, for both the owners and the District government. The Center for Housing Policy notes that "the underlying challenge for the field is that many [Inclusionary Housing] policies lack the flexibility to adapt to changing market conditions... Strengthening policies to be more dynamic in the face of unexpected price dips (or spikes) is a key area where policies can improve."[32] We believe this dynamism can come from a combination of the above recommendations and that the following three things hang in the balance: 1) the financial well-being and economic advancement of lower-income households, 2) the administrative capacity and costs for DHCD, and 3) successfully meeting affordable housing development goals. The District has a golden opportunity to make the ownership side of Inclusionary Zoning not only work, but excel.

Appendix I

From the beginning, IZ ownership, specifically permanent resale restrictions, has been controversial. Opponents to permanent resale restrictions were concerned about the affect on the economic advancement of lower income households. In essence, they believed that the design of IZ ownership units took away the only asset many lower income families have, making the units more akin to rental or limited equity cooperatives. Some of the groups that came out in opposition included Anacostia Economic Development Corporation, Columbia Heights Economic Development Corporation, H Street CDC, Howard University Law Center, and Manna, Inc. Howard University Law Center went as far as threatening a discrimination law suit against permanent restrictions, claiming that it targeted and disadvantaged minority households in the District.

As application of IZ principles trickled down into other ownership development, Councilmember Michael Brown convened a taskforce on homeownership policy supported by local funding. Below is a summary of the taskforce discussions and outcomes.

1. **Timeline**
    - **July 2010 -** Former Councilmember Michael Brown's Committee of Housing and Workforce Development convened a taskforce consisting of 30 affordable housing experts and local government officials to explore long-term affordability restrictions associated with DC-funded affordable homeownership programs.
    - **October 2010 - November 2011 -** The taskforce met 5 times, exploring the various facets of resale restrictions and examining the fiscal impact various models would have on homebuyers and the city government. Those models included shared appreciation/appraisal-based resale formula, AMI resale formula, Affordable Housing Cost resale formula, Recapture and recycle.
    - **2012 -** Since it was concluded by the majority of the working group that the District had different types of "markets" within the City, Councilmember Brown's office drafted the Affordable Homeownership Preservation and Equity Accumulation Amendment Act of 2011, which introduced different resale restricted periods, with a permanent recapture and recycle provision. The legislation was then passed to the Mayor's Housing Task Force.
    - **2013 -** The Task Force did not make a specific recommendation on the legislation. In April 2013, the Coalition for Nonprofit Housing and Economic Development came to consensus on supporting the legislation, adding that developers were free to

add other covenants and had the right of first refusal. CNHED is working to bring this to the City Council.

2. Why neighborhoods are treated differently

It was decided that a neighborhood like Columbia Heights had a completely different income/marketability/ and social appeal to it than a neighborhood like Ivy City. As a result, a uniform policy would not work for both areas. The group defined areas as "distressed" or "non-distressed" neighborhoods.

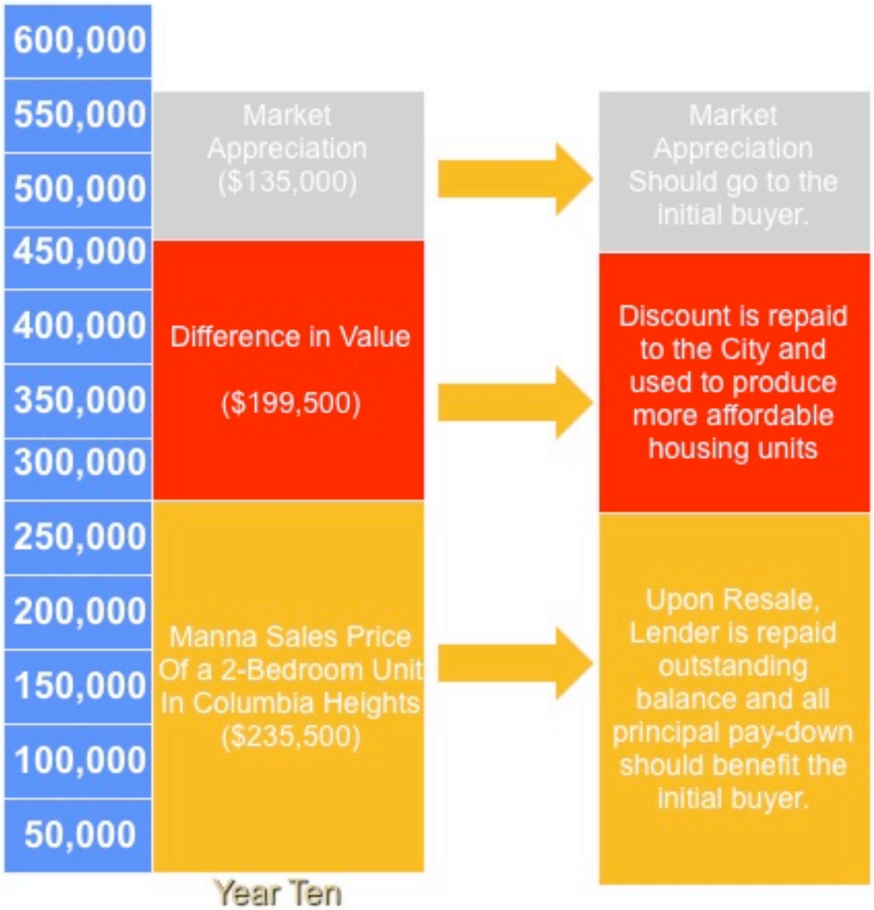
Defining what a distressed neighborhood is based on the demographics of the neighborhood. Upon examination of the various census tracts, it was found that the majority of tracts that have a 20% poverty level or higher also had a homeownership rate of 42% or lower. This became the definition of what a distressed neighborhood is.

Finally, it is difficult to sell restricted units in general, and especially in distressed areas. Market rate units have fallen in price in many distressed neighborhoods. Few buyers are going to pay just a little less than what is on the market and accept the current long-term restrictions. Affordable housing developers are backing themselves in a corner, and the homebuyer is getting very little.

3. Affordable Homeownership Act of 2011

- **Option A. – Distressed Market: 5 Year Resale-restricted period with a permanent Subsidy Recapture and Recycle Provision. -** Rewarding homeowner "pioneers" with more asset appreciation in areas that are less developed. This also acknowledges the fact that certain neighborhoods need additional subsidy simply to make new construction feasible and that homeowners will not likely purchase housing units with complex resale restrictions if the price is only nominally lower than other housing units in the same neighborhood that do not have any restrictions associated with them.
- **Option B. – Non-Distressed Market: Longer-term resale period (15 year) with permanent recapture and recycle provision.** This approach would prioritize affordability preservation in areas of the city with incredibly high housing costs.

Recapture and Recycle



Endnotes

[1] *Bridges to Opportunity: A New Housing Strategy for D.C.* District of Columbia Government. 2013. http://www.taskforce2012.org/Portals/1/docs/Bridges_to_Opportunity-A_New_Housing_Strategy_for_DC-Official_Report.pdf.

[2] The District's Inclusionary Zoning program, in its entirety, can be found in Chapter 22, Inclusionary Zoning Implementation, in Title 14 of the D.C. Municipal Regulations. An online copy of the program's regulations can be found at http://www.dcregs.dc.gov/Gateway/ChapterHome.aspx?ChapterNumber=14-22.

[3] I*nclusionary Zoning Annual and 5.5 Year Report.* Government of District of Columbia. 2013. http://dhcd.dc.gov/sites/default/files/dc/sites/dhcd/publication/attachments/IZ%20Annual%20Report%202012.pdf.

[4] *At Long Last, D.C. Sells Its First Inclusionary Zoning Unit.* Wiener, Aaron. City Paper. 2013. http://www.washingtoncitypaper.com/blogs/housingcomplex/2013/07/10/at-long-last-d-c-sells-its-first-inclusionary-zoning-unit/.

[5] What the latest District Inclusionary Zoning report lacks in its calculation of resale prices is closing costs and realtor expenses; the report also assumes IZ owners would have been able to sell at the maximum resale price. For a more accurate assessment of gain on sale, see p. 16 of *Learning from Experience.*

[6] *Georgia Avenue Developer Sues City Over Inclusionary Zoning.* Wiener, Aaron. Washington City Paper. 2012. http://www.washingtoncitypaper.com/blogs/housingcomplex/2012/12/14/georgia-avenue-developer-sues-city-over-inclusionary-zoning/.

[7] Though the particular ADUs focused on in this paper have the same resale-restricted period, this is not the case for all ADUs in the city. For detailed information on these specific ADUs and the situation of ADU owners, see *Learning from Experience Affordable Homeowners in Washington, D.C.* Manna, Inc. 2012. http://www.coas.howard.edu/centeronraceandwealth/reports&publications/102012-learning-from-experience.pdf.

[8] COLA is based on the Consumer Price Index (CPI). That's the Federal Government's official measurement of inflation. Specifically, it measures changes in the prices of 80,000 goods and services, which includes the cost of rental housing. COLA is triggered when prices go up.

[9] The data used in this analysis is from two public data sources: U.S. Census and Areavibes Inc.

[10] For more information see the California Department of Housing and Community Development website at http://www.hcd.ca.gov/hpd/housing_element2/HN_PHN_regional.php.

[11] *2012 Annual Progress Report on the Implentation of the San Jose 2007-14 Housing Element.* Government of San Jose. 2013. http://sanjoseca.gov/DocumentCenter/View/13316.

[12] See the Inclusionary Housing Policy in Redevelopment Area portion of San Jose's website at http://www.sanjoseca.gov/index.aspx?NID=1306.

[13] The citywide ordinance and updates on the legal case can be found at http://www.sanjoseca.gov/index.aspx?NID=1306.

[14] For the latest in-lieu fee figures, see San Jose Government's website at http://www.sanjoseca.gov/index.aspx?NID=1306.

[15] Patrick Heisinger, Inclusionary Housing Manager, City of San Jose. Interview with Thomas Hampton. June 2013.

[16] RHNA goals for San Francisco include the entire county. This dovetails with the administration of San Francisco's Inclusionary Housing program, which is also countywide.

[17] *Regional Housing Needs Allocation (RHNA) Production Targets and Actual Production to Date.* San Francisco Planning Department. 2012. http://commissions.sfplanning.org/cpcpackets/2011_RHNA_report_transmittal.pdf

[18] *San Francisco General Plan: Housing Element, Part II.* San Francisco Planning Department, 2009. http://www.sf-planning.org/ftp/general_plan/I1_Housing.html.

[19] For links to all of this information, see the *Documents Governing and Explaining the Inclusionary Housing Program* section of the San Francisco Mayor's Office of Housing website at http://sf-moh.org/index.aspx?page=295.

[20] *San Francisco: Inclusionary Affordable Housing Program.* Wellesley Institute. 2009. http://www.wellesleyinstitute.com/wp-content/uploads/2010/03/CaseStudySanFrancisco.pdf.

[21] Mayor's Office of Housing, City and County of San Francisco. Interview with Sarah Scruggs. May 2013.

[22] See Lloyd, Carol. "Owners' dues keep going up." San Francisco Chronicle. 5 August 2007. http://www.sfgate.com/default/article/Owners-dues-keep-going-up-2526988.php, and Lloyd, Carol. "Is inclusionary zoning providing our much needed affordable housing?" San Francisco Chronicle. 25 April 2008 by Carol Lloyd on April 25, 2008. http://www.sfgate.com/entertainment/article/Is-inclusionary-zoning-providing-our-much-needed-2491071.php#page-1.

[23] Mayor's Office of Housing. Interview with Sarah Scruggs. May 2013.

[24] *Mayor Menino Convenes Housing Boston 2020 Advisory Panel.* City of Boston. 2013. http://www.cityofboston.gov/news/default.aspx?id=6143.

[25] See the *Leading the Way* section of the City of Boston's website at http://www.cityofboston.gov/dnd/pdr/leading_the_way.asp.

[26] See *Boston, MA: Inclusionary Development Policy.* Wellesley Institute. 2009. http://www.wellesleyinstitute.com/wp-content/uploads/2010/03/CaseStudyBoston.pdf.

[27] Thomas Callahan, Executive Director, Massachusetts Affordable Housing Alliance. Interview with Sarah Scruggs. March 2013.

[28] Ibid.

[29] *Condo Law's Treatment of Affordable Units Clarified.* Massachusetts Land Use Report. 2010. http://www.landusereport.com/post/1039727090/condo-laws-treatment-of-affordable-units-clarified.

[30] See *Bill H.388.* Turner, Cleon H. The 187th General Court of The Commonwealth of Massachusetts. 2010. http://www.malegislature.gov/Bills/187/House/H00388.

[31] *After the Downturn: New Challenges and Opportunities for Inclusionary Housing.* Hickey, Robert. Center for Housing Policy. 2013. http://www.nhc.org/media/files/InclusionaryReport201302.pdf, p. 12.

[32] Ibid, p. 14.