REFINED SCOPE OF WORK ECONOMIC ANALYSIS OF POTENTIAL IMPACT OF PROPOSED INCLUSIONARY HOUSING PROGRAMS ON HOUSING DEVELOPMENT IN OAKLAND

The consultant, Hausrath Economics Group, and its subcontractor, Vernazza Wolfe Associates, Inc., (together the "Consultants") shall perform the following scope of work.

PURPOSE

To assist the City in its evaluation and refinement of an inclusionary housing program in Oakland, the Consultants will complete the following:

- ◆ Undertake economic analysis to develop an understanding of the interrelationship between the components of the City's proposed inclusionary housing program (*e.g.* percent inclusionary units and affordability levels), and the feasibility of developing new market-rate housing in Oakland;
- ◆ Undertake economic analysis to identify an in-lieu fee option for the program; and
- ♦ Summarize the findings to identify the likely impacts of the proposed inclusionary housing options on the feasibility of market-rate residential development in Oakland.

SCOPE OF WORK

The following identifies the work tasks to be completed by the Consultants.

Task 1: Discuss and Refine Work Program

The first task will involve a working session with the Consultants and City staff to address the following:

- Identify and discuss the specific inclusionary program variables and assumptions to be evaluated;
- Identify assumptions for calculating an in-lieu fee option;
- Discuss the residential product prototypes to be tested; and
- Refine the work program as needed.

Based on the working session, it was agreed that this analysis will evaluate the City's current Inclusionary Ordinance proposal, as presented at the City Council meeting of October 17, 2006 and forwarded in "final" form by City staff.

Task2: Housing Project Feasibility Analysis

The purpose of the housing project feasibility analysis will be to develop market-based, pro forma cash flow models for representative market-rate residential development in Oakland and to use these models for analyzing the relative impacts on housing project feasibility of the proposed inclusionary housing requirements. The feasibility analysis will include five parts: prototype identification, market data, cost estimates, pro forma development, and sensitivity analysis to test the effects of inclusionary requirements.

Task 2a: Identification of Residential Product Prototypes

Representative housing prototypes will be identified to reflect the range of types of housing development occurring in Oakland. Consideration will be given to reflecting both housing product types (apartments, townhomes, lofts, single family), development densities (lower, mid-rise, and high-rise), and tenure types (for-sale, rental) that are representative of housing development occurring throughout the City. The prototypes will be developed based on the Consultants' familiarity with Oakland development, input from City staff, and our work with project developers active in Oakland. This scope assumes no more than six prototypes and variants.

Task 2b: Market Values/Revenues

Drawing from available market analyses and market comparables for Oakland developments, housing sales prices/rents will be identified for the residential product prototypes. As relevant, this task will identify sales prices/rents for similar unit types in different residential submarkets within Oakland. Consultants will draw from in-house data and information on prices and rents for new housing development in Oakland and from inputs available from City staff, and will gather additional information as needed from project sponsors/developers and local real estate industry representatives and publications.

Task 2c: Development Cost Estimates

Development costs including land costs will be estimated for each of the product prototypes. The Consultants will draw from actual project experience of residential developers in Oakland and nearby communities, from inputs available from City staff, and from published sources, as needed, to estimate the total development costs for the construction of new housing.

Task 2d: Model Development

This subtask will focus on the preparation of pro forma residential development cash flow models. The models will be simplified for this analysis, to focus on the key variables

affecting financial feasibility. Development costs will be combined with the estimates of unit sales prices and rents/market values to develop feasibility models for each of the market-rate housing product prototypes. The models will identify the "base case" financial picture for the prototypes, without the proposed inclusionary housing program.

Task 2e: Sensitivity Analysis

The pro forma models will be used to test the sensitivity of financial feasibility of each of the prototypes to the proposed requirements for an inclusionary housing program. The analysis will focus on testing the following key program variables:

- Percentage of affordable units;
- Affordability levels; and
- On-site, off-site, and in-lieu fee options (see Task 3 below).

Effects on the financial feasibility of development will be evaluated in terms of the significance of the effects of proposed program requirements, and with particular focus on the extent that potential requirements could be significant enough to affect the production of new housing. Any significant variations in financial feasibility among residential prototypes and/or submarkets will be identified. If the proposed requirements are found not to be feasible, the analysis will identify those program variables that have the most effect on project feasibility and identify program options that could be feasible.

Jointly with City staff, consideration also will be given to whether there are other policies that the City might adopt to enhance financial feasibility and offset the effects of inclusionary requirements.

Task 2f: Conclusions of Feasibility Testing

The results of the sensitivity analysis will be summarized to identify the inclusionary program variables tested and their likely impacts on the feasibility of residential development in Oakland. The results will be summarized and discussed at a working session with City staff.

Task 3: Costs of Inclusionary Requirements and In-lieu Fee Option

The proposed inclusionary requirements can be met on-site, off-site, and/or through payment of an in-lieu fee. This task will identify the "costs" and other aspects of each of these options from the perspective of the market-rate project that would be subject to the requirements. These "inclusionary costs" will be used to test the impacts of the proposed requirements in the sensitivity analysis described above (Task 2e). The subtasks below will address each of the options for meeting the proposed inclusionary housing requirements.

Task 3a: Affordable Prices/Rents for On-site Inclusionary Housing and Possible Cost Differences

If the inclusionary units are provided on-site as part of the market-rate housing project, the "costs" to the market-rate project primarily result from the differences in revenues between the affordable units and the market-rate housing. This task will identify the affordable sales prices and rents for the inclusionary units, and consider whether there would be any differences in development costs that should be accounted for in the sensitivity analysis (Task 2e).

- Identify affordable sales prices and rents (as relevant) for on-site inclusionary housing, based on the affordability levels in the proposed ordinance. Use standards identified in the proposed ordinance and by current City programs. This analysis will cover prices/rents for studios and one-, two-, three-, and four-bedroom units.
- Consider whether there would be any differences in development costs for the inclusionary units that should be accounted for in the sensitivity analysis, drawing from work under Task 3b below.

Task 3b: Costs of Off-site Inclusionary Housing based on the Housing Affordability Gap

This subtask will develop up to two affordable housing prototypes for meeting inclusionary requirements off-site and identify the difference between what a household can afford to pay and the development costs of a new unit. This gap will define the 'cost' of the off-site option to the market-rate housing project.

- Drawing from Task 3a above, identify affordable rents and sales prices based on the affordability levels in the proposed ordinance.
- Define rental and ownership prototypes that could be built off-site to satisfy developers' inclusionary requirements.
- Develop overall development costs for each prototype by bedroom size, including land costs. Compare with costs for market-rate prototypes under Task 2c above to assure consistency and evaluate differences as being reasonable.
- For ownership housing, estimate the differences between affordable sales prices and development costs.
- For rental housing, determine the subsidy per unit that would be needed based on the cost of development that could be supported by net operating income available for debt service.

• Summarize the losses or "gap" to be paid by the private development to meet the off-site inclusionary housing requirements. The losses will be identified consistent with the number of bedrooms, for studios and one-, two-, three-, and four-bedroom units.

Task 3c: In-lieu Fee Option

The Ordinance proposes an in-lieu fee option to be based on the full subsidy required for the City to provide the off-site inclusionary units. This subtask will identify the fee based on the analysis under Task 3b above, and assuming development costs consistent with prevailing wage requirements.

- Draw from the analysis of the gap between what a household can afford to pay and the development cost of a new affordable unit to identify the in-lieu fee payment required to meet the off-site inclusionary requirements. Up to two development prototypes will be analyzed, based on costs reported by affordable housing developers in the most recent NOFA submissions. If two prototypes are analyzed, then the gap will be an average of the two prototypes.
- Calculate gaps for both ownership and rental housing. Compute an average gap figure.
- Identify the in-lieu fee by unit size in terms of number of bedrooms.

Task 4: Developer Consultations

The Consultants will confer with selected residential developers to review and discuss assumptions for the financial analysis and findings regarding the impacts of inclusionary program requirements on market-rate housing project feasibility. It is anticipated that City staff will confer with housing advocates, to review and discuss the preliminary findings of the financial feasibility analysis.

Task 5: Refine Analysis

The economic analysis will be refined as needed, based on inputs from City staff and from the consultations with developer and housing advocate representatives.

Task 6: Written Report

A written report will be produced at the culmination of the economic analysis. The written product will be a summary report, identifying the inclusionary housing program requirements considered and their potential impacts on market-rate residential development in Oakland. The report also will summarize the analysis to provide documentation for the in-lieu fee option. The report will include a user-friendly executive summary and a technical appendix, if needed.

A draft report will be produced for City staff review, and a final report prepared incorporating inputs and responses to comments received from City staff on the draft document. The Consultants will supply City staff with camera-ready originals and electronic versions of the draft report and final reports, and with up to five bound copies of each document. It is assumed that additional copies of the draft and final reports will be produced and made available by the City.

Task 7: Meetings/Working Sessions

This scope of work assumes that the Consultants will participate in three meetings/working sessions with City staff during the course of the economic study. These meetings will include the following:

- An initial scoping and brainstorming meeting to discuss the residential
 product prototypes and the inclusionary housing program variables to be
 tested in the financial feasibility analysis, and to further review and refine the
 work program;
- A second session to present and discuss findings concerning the base case feasibility analysis and the costs of the inclusionary requirements, at the completion of Tasks 2a-2d and Task 3; and
- A third session to present and discuss findings of the sensitivity analysis, at the completion of Tasks 2e and 2f.

