FEDERAL RESERVE BANK OF SAN FRANCISCO

California Post-RDA
Affordable Housing Developer Survey

Analysis of Results – December 7, 2015

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The views expressed herein do not necessarily reflect the views of the Federal Reserve Bank of San Francisco, the Federal Reserve System, or Housing California.

Issue Background[1] and Survey Purpose

California's 400-plus Redevelopment Agencies (RDAs) played a critical role in the development of affordable housing across the state for over 60 years. Created to address the state's community needs after World War II, redevelopment agencies allowed cities and counties across California to recapture growth in property taxes as tax-increment financing for affordable housing and community infrastructure projects, to improve conditions in designated areas within their jurisdictions that faced blight and disinvestment. By 2008, RDAs were receiving 12 percent of the state's annual property tax revenues. Infrastructure uses of RDA funds included such activities as site remediation, economic redevelopment, and development of community parks and facilities. RDA funds were frequently used to support affordable housing development projects; between 2001 and 2008 alone, 63,600 new units were funded in part by RDAs, nearly half of them targeted to be affordable to those earning 50 percent or less of the area's median household income. With the passage of new legislation in 1976, each agency was required to set aside 20 percent of its RDA dollars in a Low and Moderate Income Housing Fund (LMIHF) to be used only for affordable housing efforts. It is estimated that these LMIHF dollars collectively amounted to just over $1 billion per year by 2010.

California Governor Jerry Brown proposed the dissolution of RDAs in January 2011 as part of a larger measure to reduce the state's budget deficit and cover general fund expenses, estimating that eliminating RDAs would recapture roughly $1.7 billion per year in property tax revenues for the state. Despite a prolonged policy effort over the course of the 2011 Legislative session to temper the governor's proposal and save or redesign RDAs in some form through legislation, the RDA program and its agencies were ultimately dissolved in 2012. Other local agencies (typically housing authorities or city or county housing departments) were subsequently designated "RDA successor agencies," responsible for ensuring that existing RDA funds were distributed to all of the housing and infrastructure projects to which they were already promised, but no additional funding would be awarded through RDAs to new projects.

Over ninety percent of all affordable housing development projects utilize LIHTC funding . . .

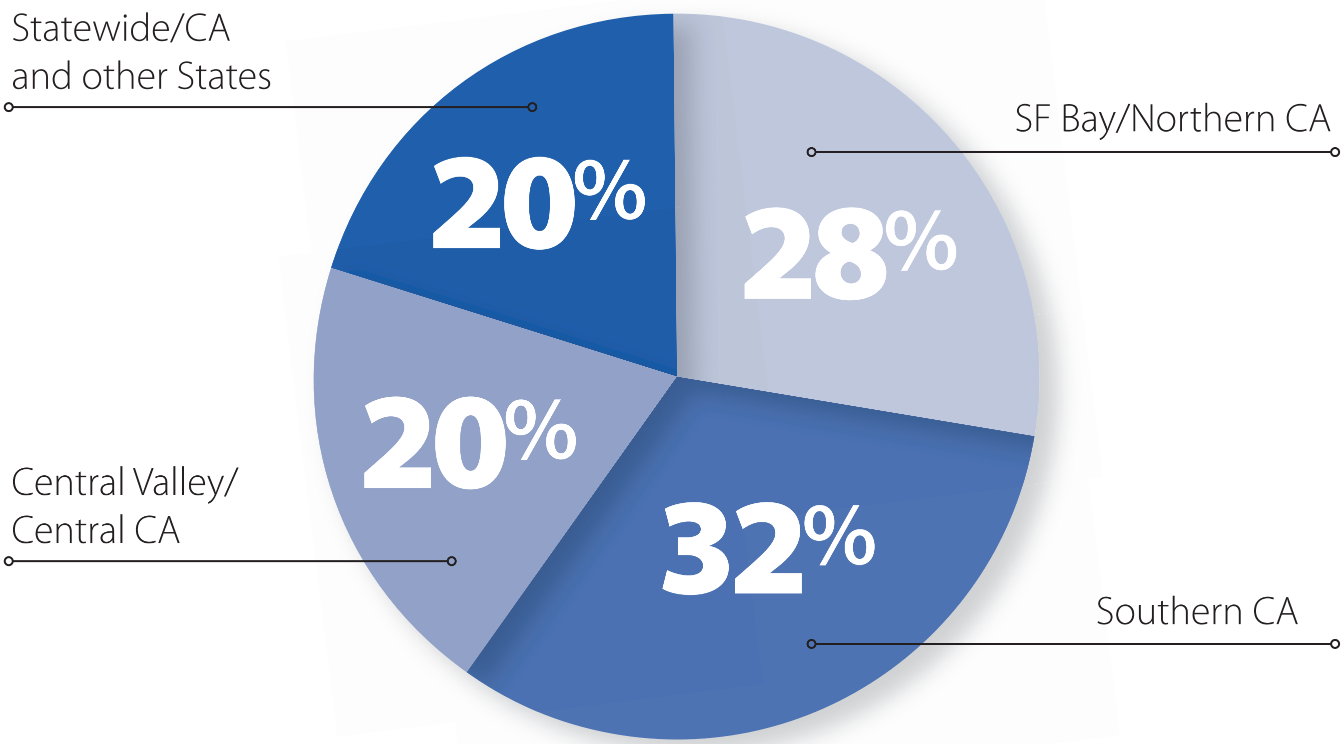
RDA dissolution was widely expected to have significant impacts on California affordable housing developers' ability to produce new projects for several reasons. RDA funds were seen as an important commitment of local resources to an affordable housing project, which demonstrated local government support of the proposed housing and was often used to leverage more significant amounts of funding for a development through the federal Low Income Housing Tax Credit (LIHTC) Program. RDA dollars were also a common source of gap financing for LIHTC-funded projects. Over ninety percent of all affordable housing development projects utilize LIHTC funding, and the majority of developments awarded 9% LIHTC credits in California in 2011 included RDA funds in their proposed development financing deals. Additionally, the redevelopment program was a longstanding and heavily-used source of funding for affordable housing in California, seen as a relatively stable and reliable resource as other affordable housing funding sources were frozen or cut during and after the 2007-2009 national recession.

Three years after the unexpected loss of a significant affordable housing funding source in California, the Federal Reserve Bank of San Francisco's Community Development Department surveyed the state's affordable housing developers in October 2015 to learn how they are faring following RDA dissolution; how their development pipelines have been affected by the loss of RDA funds; and how new legislation, local regulation, or funding strategies have impacted affordable housing development in California over the past three years. This survey was a joint effort with Housing California, a statewide affordable housing organization, and was distributed to public, nonprofit, and for profit developers of affordable housing across the state. Here we present an analysis of the current conditions and challenges expressed in the survey responses of 71 affordable housing development organizations across California.

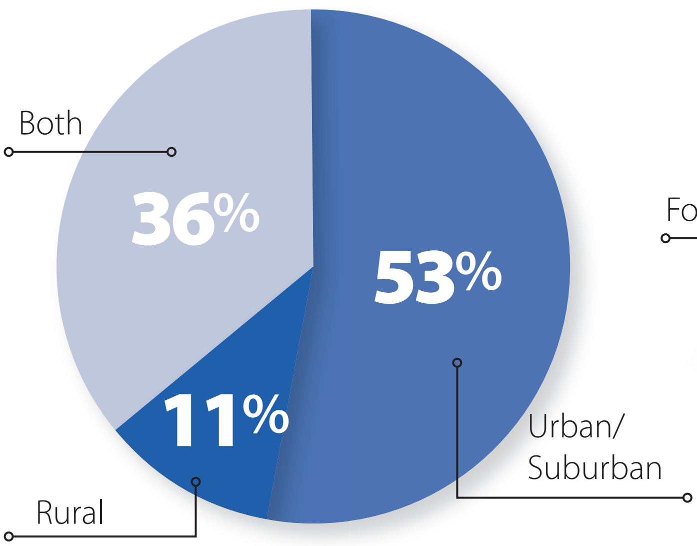
1 For a detailed discussion of RDAs and their dissolution, see: Casey Blount, Wendy Ip, Ikuo Nakano, and Elaine Ng, "Redevelopment Agencies in California: History, Benefits, Excesses, and Closure." U.S. Department of Housing and Urban Development, Office of Policy Development and Research, January 2014. http://www.huduser.gov/portal/publications/Redevelopment_WhitePaper.pdf Statistics cited in the above issue summary have been drawn from this white paper.

Respondent Information

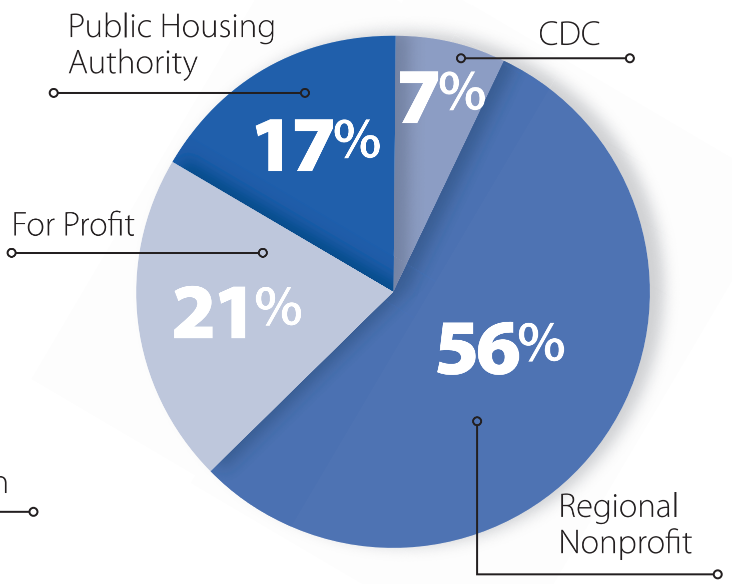
Primary Development Area



Urban, Suburban, or Rural Development Areas



Developer Organization Type



Source: FRBSF/Housing California Affordable Housing Developer Survey, 2015

Summary of Preliminary Survey Responses from Developers

90% have seen an **increased need for affordable housing** in their markets over the past three years

80% report that their pipeline projects have been **negatively impacted by rising cost of land** acquisition and/or site remediation and readiness

65% have used or will be applying for **new post-RDA sources of federal or state funding** in upcoming projects

62% report that **changes to the unit mix** of their pipeline projects had to be made after RDA dissolution for funding reasons

61% say that their organizations have **had to reduce staff** or make other organizational changes as a result of funding reductions

42% say that **new state or federal legislation has impacted** their organization's development work since RDA dissolution

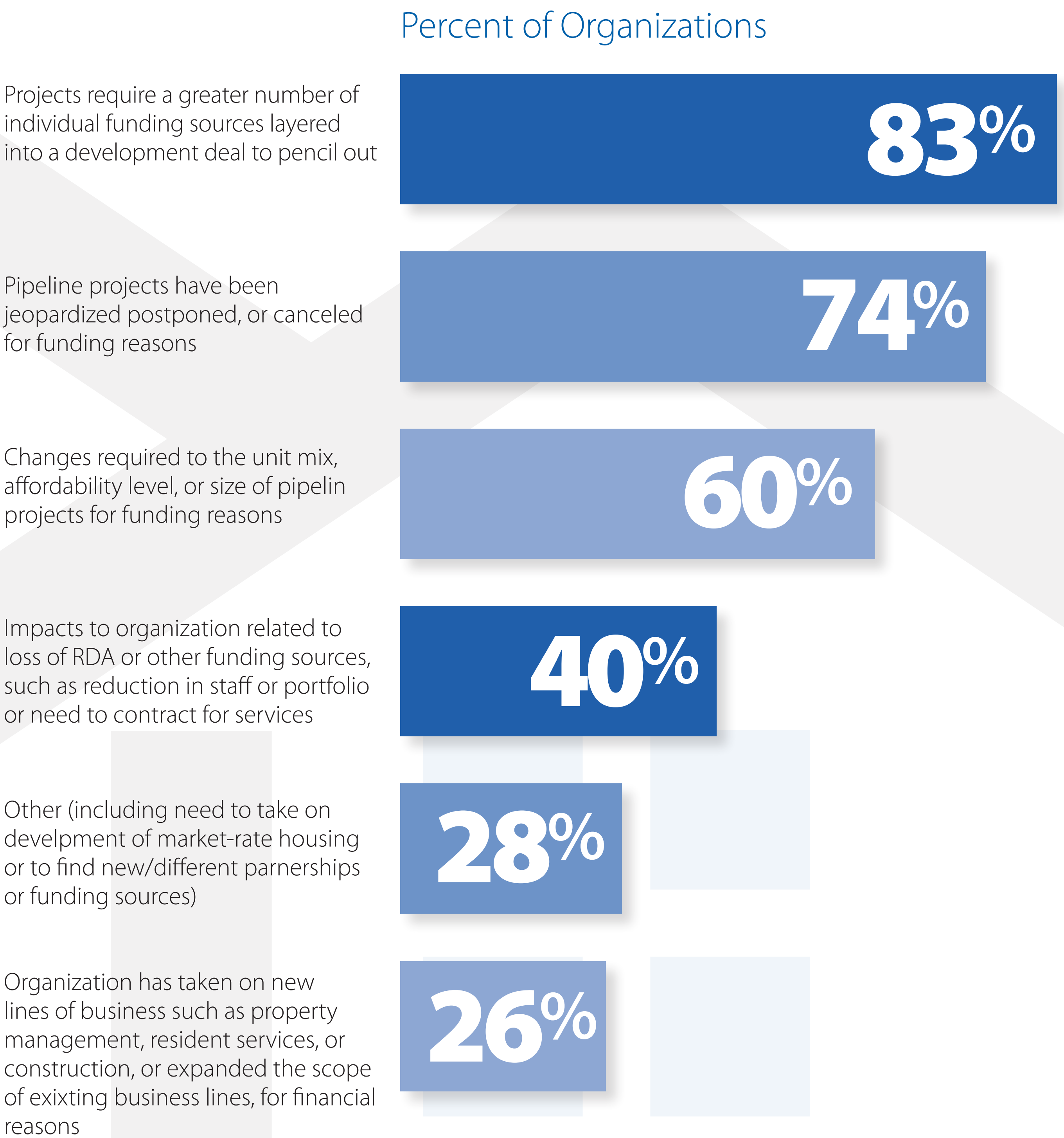
41% note that their organizations **have taken on new or expanded lines of business** beyond affordable housing development for funding reasons

26% report that jurisdictions in which they develop affordable housing have introduced **post-RDA regulatory reforms**

22% report that jurisdictions in which they develop affordable housing have introduced **new funding sources** to replace RDA funds

18% are exploring new **private or other non-state or federal sources** of funding for future projects

Organizational Impacts of RDA and other Funding Losses



Source: FRBSF/Housing California Affordable Housing Developer Survey, 2015

Detailed Findings Drawn from Responses

Overall Impacts

Developer respondents note that the timing of the RDA loss is important, because it compounded an already difficult development environment following the recession. Without RDA funds to cover gap financing and without a replacement in sight for a depleted 2006 state housing bond program, developers are turning to other local sources of funding for gap costs such as public housing authorities; yet these local agencies are also running low on financing dollars for new projects and contending with uncertainty around future funds. New construction projects are more difficult to fund without RDA, respondents say, so they are turning to more acquisition and rehabilitation projects. Some developers are also taking on smaller projects which require less overall funding but also result in lower developer fee returns and less cash flow.

New Local Funding Sources ("Boomerang Funds")

Some jurisdictions have created so-called "boomerang funds" – local redevelopment-style tax-increment funding sources for affordable housing – including Alameda, Contra Costa, Los Angeles, Santa Clara, and San Mateo Counties; the City and County of San Francisco; and the Cities of Oakland and Santa Clara, among others. However, respondents explain that none of these sources seem to be large enough to replace the amount of RDA funding previously available, and it is also unclear at this point how much funding these sources will provide over time. These sources have only recently been introduced, so most of the respondents in our survey said they are aware of the new sources but have not yet applied for or received such funding.

New State, Federal, and Private Funding Sources

Several developers mentioned the new California Affordable Housing and Sustainable Communities (AHSC) funding program, also known as cap and trade funds, and expressed interest in applying for these funds for upcoming projects. However, some developers noted that it will be difficult for rural projects to be competitive within this program, and just 10 percent of AHSC funds are reserved for rural areas only in the draft program regulations available for comment at the time of this survey. Others who develop housing mostly for the working poor in areas that are not designated "disadvantaged communities" per the program regulations said this program would not be accessible to them either. In rural and suburban areas that do not already have high-quality transit, the funds must be used in part to develop a transit stop and establish other strategies to reduce vehicle miles traveled, but development of affordable housing is not a mandated use of funds. By contrast, in urban areas with existing high-quality transit, the program mandates that funds be used in part for affordable housing development. Additionally, this program carries with it many new requirements about how the funds need to be used, which can add costs, according to respondents. The California Strategic Growth Council recently held forums for public comment on the draft AHSC regulations, suggesting that some of the regulations making it difficult to use AHSC funds in certain areas may be adjusted. Some developers also noted that they would be applying for funds from the new Veterans Housing and Homelessness Prevention (VHPP) Program, as veteran and veteran family housing are both state housing priorities with dedicated funding.

A few respondents said their organizations are now exploring private funds for affordable housing, such as bonds sold to individual investors, capital campaigns, and joint ventures with for-profit developers who provide land and other resources. Respondents noted that most of these private sources are small and/or targeted toward specific uses such as preservation of existing affordable units.

Cost of Land, Labor, and Geographic Factors

Many respondents confirmed that RDA loss is significantly impacting site acquisition. In the past, the cost of acquisition was typically covered by public sources – often redevelopment funds. Respondents explained that they are now more frequently competing with market rate developers for land, especially in metropolitan areas where the costs of land and housing are rising sharply. Respondents note that it is very difficult for them to outbid these market rate developers without RDA funds for site acquisition, so they are more likely to be diverted to less-desirable sites that are more affordable in land costs, but are often difficult-to-develop areas (DDAs) that end up adding costs in site readiness and remediation. Certain cities seem less likely to donate land given the competitive market for all developers, some respondents observed. Regulations, fees, and fines around site acquisition and infrastructure were also frequently mentioned in responses as affordable development barriers in some areas, and some respondents pointed out that infrastructure costs in particular are more difficult to cover without RDA funds. Several respondents also cited the difficulty of competing with market-rate developers not only for the prices they can pay, but also their ability to close quickly on a land purchase and to pay in cash, which affordable housing developers cannot do. Respondents explained that in some areas where a jurisdiction previously may have gifted the publicly-owned land needed for an affordable housing project to an affordable housing developer, the jurisdiction is instead opting to go with market-rate buyers who can pay more for the site with fewer strings attached. In some cases, respondents said that not having RDA funds to cover gap financing needed for land expenses made it impossible for them to compete in California, and pushed them to seek sites outside the state instead where land costs are lower and there are fewer regulatory hurdles. As one respondent explained, land costs are so high and the market for them so competitive in California that "we have taken our development experience and money to other states who welcome us with open arms and require lower project costs in exchange for fewer regulations."

Respondents also pointed to the high cost of land around transit stations – light rail stations in particular – as a problem for affordable development, in part because transit-proximity is highly valued in competitive affordable housing funding programs like LIHTC. Labor costs were another issue mentioned, as affordable housing subsidy programs often mandate that developers pay construction workers prevailing wages in California. Finally, the drought is a newer issue adding to development cost, according to one developer, because of increased water rates in developments. All of these issues have become more troublesome for affordable housing developers without RDA funding to cover gap costs.

Respondents working in smaller cities or remote rural areas also noted that the realities of their geography – small, widespread populations and infrastructure and transportation challenges – make it very difficult for them to compete for funding or favorable regulation changes that would help their regions. They explain that they often lose out for any workable funding as overall subsidy dollars dwindle in California and competition grows.

Local, State, and Federal Regulations

Respondents explained that a few jurisdictions are offering streamlined approval processes and fee waivers for affordable housing, but say that it would be helpful for more jurisdictions to do so. Others say that some of these streamlined measures are not working well in practice in keeping costs down, and even where they have been effective, they do not make up the overall loss of RDA funding. In fact, there is a strong consensus among responding developers that new regulatory measures and new programs at the state and federal level are too small to have significant impact in covering development costs, and do not go far enough to make up for the overall RDA loss. At the same time, some respondents note, these new programs and policies also come with new compliance rules that can add to project cost. Several respondents stressed that the combination of increased regulation and fewer funding dollars is making it much more difficult to produce or rehabilitate affordable homes in California.

Unit Type and Mix

Low-income family units have been most at risk post-RDA, according to respondents. Most developers said that they are either moving toward specially-targeted projects like special needs or veterans' housing, because population-targeted program funding is among the only non-LIHTC funding available now. Several respondents said that they have had to convert proposed projects to predominantly market-rate units (such as "80/20" deals, where only 20% of the units are affordable) to make projects pencil out. One developer said, "We reduced a family apartment complex (low and very-low income units) from 80 units to 40 units. We are now going to build 13 single-family homes [instead] that will be priced at moderate-income level;" another respondent explained that "in order to match up with the funding sources, we had to reduce the unit count from 77 to 50 units on a project recently started." Large family units are the most expensive to build, respondents explained, so they are much less likely to be included in affordable housing development now despite increased need for this type of unit in some markets. Overall, they note, affordable units are being sacrificed in favor of market rate units just to make deals pencil out. "We are often forced to build what will be most competitive for [low income housing] tax credits and not what is most suited for the area or population," one developer explained.

Organization Impacts

After RDA dissolution and other funding cutbacks, some affordable housing developers are taking on more property management opportunities or other new lines of business such as single-family development, consulting, and joint ventures with for profit developers, in order to stay in business. Others are taking their business out of state, according to respondents. In some areas, public housing authorities have been designated the RDA successor agencies, and some respondents from these organizations note that they are being asked to do more work on more sites to cover these successor responsibilities without any added funding for staff and operations costs.

Moreover, over half of the respondents said that their organizations have had to cut staff due to reduced funding – some by as much as 30 to 50 percent of their total personnel. Also taking into account the significant number of housing professionals who lost their jobs in 2012 in RDAs across the state when these agencies were dissolved, only some of whom were reabsorbed into other affordable housing roles elsewhere, many respondents observed that the past few years have been devastating to organizational stability and staff retention and development. Many emphasized that they have to do more with fewer staff resources, and in some cases salaries have been reduced to retain talented employees. One developer said, "The Director of Housing Development position has been left open for about two years because our pipeline is small, uncertainty is high, and I don't know if we'll earn enough developer fee to cover that relatively expensive position."

Affordable Housing Need

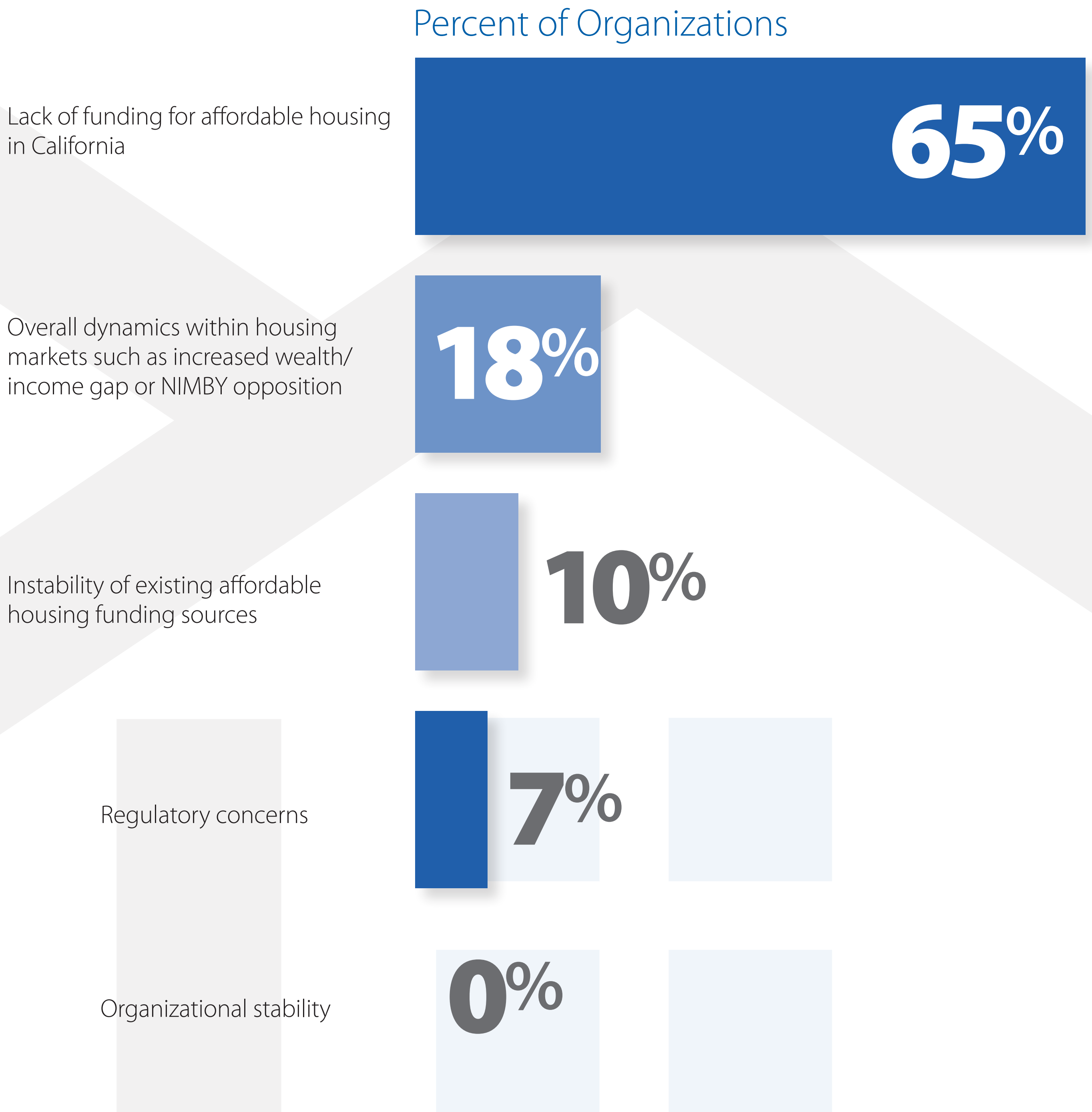
Fully 90 percent of developer respondents reported that the need for affordable housing has increased in their markets in the past three years. One noted that "there are over 5,000 families on our waiting lists," while another said, "we are opening a new 40-unit development in 2016 and we have over 450 people on an interest list for it." Several respondents have observed a much higher number of homeless individuals and families in their markets – one said the 2015 point-in-time homeless count showed a 45% increase in homelessness in their area over the previous year. In areas where many residents work in the tourist economy and earn low wages, respondents said, the jobs-housing imbalance is very high and rent-controlled units are at risk when they turn over. One respondent said, "There are not enough affordable housing options to cover the need, especially that of very low income families with no special need outside of living at poverty level." Some regions that have seen significant population growth without accompanying housing production face a severe housing crunch, as one respondent explained: "Our community has underdeveloped housing related to the growth rate (approximately 2 percent/year) and the vacancy rate is now less than 1.5 percent – less than 0.75 percent for one-bedroom units." With so many new funding programs focused on specific populations, developers note, they are struggling to serve increased need among poor families.

Concluding Comments

Developers responding to our survey repeatedly emphasized that affordable housing funding and programming are not just about building homes. Many affordable housing developments include supportive services for residents that are much more difficult for these individuals to find with fewer and fewer affordable units available in the face of increased need. The respondents see stable housing and services as closely intertwined and critical to stabilizing residents and lifting them out of poverty. When significant funding sources like RDA are lost, respondents explain, it also impacts the stability of affordable housing organizations as noted above, and their ability to consistently provide housing and services just as the need for affordable homes is increasing dramatically across the state. As one respondent observed, "We need development dollars, but we also need resident service dollars. Low-income families and those with special needs need case management to help them stay housed. Developing one without the other is not addressing the root causes of poverty."

In conclusion, many respondents emphasize that a "permanent source" of affordable housing funding in California is needed to replace RDA funds, produce a much greater volume of needed affordable homes in communities across the state, and reduce uncertainty in the development process.

Greatest Affordable Housing Development Concern Going Forward



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