The Economics of Land Use

Executive Summary

Park City UT Housing Review

Prepared for:

City of Park City, Utah

Prepared by:

Economic & Planning Systems, Inc.

Date

EPS #153048

Economic & Planning Systems, Inc.
730 17th Street, Suite 630
Denver, CO 80202-3511
303 623 3557 tel
303 623 9049 fax

Denver
Los Angeles
Oakland
Sacramento

www.epsys.com

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1. EXECUTIVE SUMMARY

1.1 Summary of Findings

The following are the major findings from EPS's work. Each frames the context in which the recommendations are structured.

1. ***The gap between market rate housing and prices affordable to the City's workforce continues to widen.***
   - Single-family housing prices have escalated an average of 6.7 percent per year since 2000, even factoring in the recessions. From 2010 to 2015, prices have escalated at 10.7 percent annually from approximately $990,000 to nearly $1.5 million for a single-family home. Furthermore, since 2000 condo prices have increased at 5.5 percent per year from approximately $365,000 to more than $684,000, although most of this increase is attributable to the escalation of prices before the housing market bubble.
   - Median incomes have increased just 1.7 percent annually since 2000, and qualifying income limits have increased 1.9 percent annually since 2000.
   - The "affordability gap" has widened more than two-fold from approximately $375,000 to $949,000. That is, in 2000 a household earning Park City's median household income ($65,800) could afford a house at $180,400 and the average-priced single-family house sold for approximately $555,000. By 2014, a household earning Park City's median household income (according to the U.S. Census' 5-year estimate of $89,886) could afford a house at $365,900 and the average-priced single-family house sold for approximately $1.3 million.

2. ***There is dwindling inventory of housing affordable to the community workforce.***
   - Other studies and needs assessments have also sounded the alarm. There is a dwindling stock of housing affordable to those who work and would live in Park City if they could afford it.
   - In 2000, 26 percent of the City's for-sale inventory was valued at less than $300,000. By 2014, that portion had dropped to 12 percent. Over a shorter period of time, between 2011 and 2014, the portion of for-sale inventory affordable to a household earning median income dropped from 21 percent to 17 percent.

3. ***The existing housing resolution (13-15) applies to less than 50 percent of all residential development activity.***
   - Approximately 78 affordable units were built between 2005 and 2011 under the current housing resolution. As these were the units to meet the 15 percent inclusionary zoning requirement, it is estimated that they were based on projects totaling 520 total units. During those 6 years, however, there were 1,100 residential units permitted, indicating that the inclusionary zoning requirement applied to approximately 50 percent of all residential construction.

4. ***Had the intent of a previous version of the housing resolution (version 6-94) been followed, nearly double the number affordable units might have been built.***
   - Among other things it established, resolution 6-94 expressed the City Council's intent to consider whether the future version of the resolution's housing requirements should apply to residential development of more than two units.

5. ***Moving forward, the development pipeline would suggest that there are fewer applications that will apply to the existing housing resolution.***
   - According to staff, there are few if any opportunities for future annexation, and only three master-planned developments (MPD) are known. Development is increasingly infill and single-site demolition/rebuild.

6. ***Revisions to the housing resolution have focused increasingly on the community's workforce.***
   - In a revision to the housing resolution in 1999, the City Council listed that the beneficiaries of such policy should include police, teachers, firemen, service workers, and longtime community residents. By 2006, that had been expanded to include: those who live and work in Park City, "essential" public and private sector service workers (schools, fire, municipal corporation, sewer district), full-time employees of businesses located within city limits, residents of Park City for the past 24 months, owner or owner's representative of a business within city limits, senior citizens, and the physically or mentally challenged. In a subsequent revision, the word "essential" was removed from the public and private sector service workers category.

7. ***Moreover, while improvements have been made to the housing resolution, these changes have had decreasing returns given the changing market.***
   - Over time, improvements, clarifications, and modifications have been made to the housing resolution, although some of its elements have not; e.g., the per-unit incentive of $5,000 has not been updated since 1991. MPDs and annexations were more common in the early 1990s than they are now, and they do not provide the same vehicle for affordable housing production they once did.

8. ***There are conflicting policy objectives regarding height, view-shed, historic preservation, and open space.***
   - As has been pointed out in previous studies, these desirable planning objectives conflict with the objective of achieving greater housing affordability. They all serve to exacerbate affordability conditions and increase prices by generally decreasing the supply of housing.

9. ***EPS employee generation survey data for Park City are generally in line with the current factors in the existing housing resolution.***
   - The commercial mitigation portion of the current housing resolution bases its mitigation requirement on 20 percent of the 4.4 full-time equivalents (FTEs) generated per 1,000 square feet of commercial space. Based on analysis and vetting of 132 survey responses from Park City employers, the overall rate is currently estimated at 3.9 FTEs per 1,000 square feet for the City.
   - The information collected provides sufficient detail to replace the existing types of rates with City-relevant numbers as well as differentiate between, for example, a full-service

restaurant (8.1 FTEs per 1,000 square feet) and a quick-casual or fast food restaurant (6.9 FTEs per 1,000 square feet).

- Many categories were within approximately 20 percent of the current generation rate, such as lodging (0.5 FTEs per room versus the existing 0.6 FTEs); medical profession/health care (2.7 FTEs per 1,000 square feet versus the existing 2.9); finance/banking (2.8 FTEs per 1,000 square feet versus the existing 3.3); education (2.2 versus the existing 2.3 FTEs); and real estate and property management resulted in the same generation rate (5.9 FTEs).
- One category was different by more than 20 percent of the existing generation rates, such as "other professional services" (2.7 FTEs versus the existing 3.7 FTEs).

1.2 Recommendations

1. ***From a development-based approach, Park City should consider providing additional financial or economic incentives.***
   - A first consideration concerns the development of rental units. To address this need, the City could consider deferring, abating, or granting back some portion of local property taxes to property owners/managers for keeping units in long-term affordability. From one perspective, and because 9 percent low-income housing tax credit (LIHTC) allocations are so limited, it might be worthwhile to explore this tool as a way to "fund" additional housing without necessarily having to generate funds. In such a case, there are a number of communities that have established such a mechanism to very effectively incent the development of affordable rental units. The City could decide what level of affordability (e.g., a percent of the affordable workforce wage) and what term (e.g., units remain affordable at specified income level for 15 to 30 years) to require. This technique could be applied to new and rehabilitated rental properties. (This recommendation needs to be considered within the City's legal authority.)
   - As it concerns for-sale housing, the City should consider whether the per-unit fee waiver, currently a part of the existing housing resolution, is worth maintaining. Because the gap between market rate and affordable units is so great (currently estimated at nearly $950,000), the $5,000 per unit waiver of fees is not enough to motivate a developer; it is therefore, largely symbolic. At a minimum, the City should consider having a discussion about waiving either 100 percent or some substantial portion of permit and impact fees. (In context, the fee waiver was set at $5,000 in 1991. In today's dollars, it would need to be approximately $8,600 to have at least the same value.)

2. ***The City should modify the commercial component of the housing resolution.***
   - <u>Policy Context</u>: From the perspective of a policy modification, it is always possible to convert this commercial mitigation strategy into an actual commercial linkage program—i.e., using a nexus study to establish fees that are assessed to new non-residential developments on a per-square foot basis by land use categories. EPS believes that the current version of a "commercial mitigation strategy" generally achieves the same outcomes as a commercial linkage program might, and that the magnitude of units built or in-lieu fees collected would be roughly equivalent. Like the survey data collected in this study, a nexus study also collects data to identify the number of FTEs generated by different non-residential land uses. It quantifies the distribution of jobs by occupational category and assigns them to wage levels. The workers (and their households) are distributed by median income categories, from which it can be estimated what portion of

all jobs created by the new non-residential development require housing assistance. The fee is calculated as the affordability gap, or the difference between the market rate and price of an affordable housing unit to particular households by median income level. The total affordability gap for the lower-income households is estimated and divided by the total square feet of a development to determine a per-square foot fee.
Generation Rates: The City should discuss the merits of incorporating the new survey-based employment generation rates. It should be acknowledged that this type of basis for calculating employment generation rates is always subject to a margin of error. On one hand, asking employers the number of their full-time and part-time staff relies on the accuracy of the information the person surveyed has available. On the other hand, it relies on the respondent's knowledge of the total floor area of their space, and in the absence of that (which is very common), the accuracy of this part of the information is reliant on either the respondent's or the data-gather's ability to accurately gauge the size of the space. EPS made every attempt to fully vet the numbers given to all data-gathers in the survey work. We cross-checked the square-footage numbers against Summit County Assessor data.

- Mitigation Rate: Aside from the 15 percent residential set-aside requirement, there are a couple other factors that seem to be associated with mitigation of affordable housing need. On one hand is the 20 percent mitigation factor applied to the commercial component; on the other hand is the 34 percent "location substitution" factor identified and both require the mitigation of some portion of the housing demand generated by those uses. In the case of the City's current resolution, 20 percent appears to have been chosen as a number reflective of the portion of FTE-based households in need of housing assistance, though no documentation is available to confirm this.

  In the case of the 34 percent location substitution factor, it appears through research that this number originated from an analysis of 2005 commuting data that identified 34 percent of the City's jobs were held by City residents. It was held that this was an optimal number to maintain and has been applied to estimates of affordable housing demand since then. In the context of other resort communities, this number is often a policy-driven factor. Telluride (CO), for example, chooses to require a 40 percent commercial mitigation rate; San Miguel County (CO) requires 15 percent; Vail (CO) requires 20 percent; Jackson Hole (WY) requires 35 percent; and Aspen (CO) requires 60 percent. These rates are not necessarily based on any specific analysis of in- and out-commuting patterns; they are based on community priorities. As such, Park City should engage in a discussion with elected officials about an appropriate "goal" for housing local workers. By way of comparison, if Park City did embark on a nexus study to quantify the jobs-housing linkage for commercial development, this mitigation rate would be a factor developed in the analysis, which then becomes, for communities with such policy, the subject of policy debate and community goals.

- In the end, no matter which direction the City takes on this issues, it needs to have a discussion about what percent of its workforce it believes should live locally and start to frame the analysis of other production goals around it.

3. The City should modify its in-lieu fee structure.

- The current housing resolution establishes a structure based on three pieces of information: 1) the median market value per square-foot of 600 to 1,600 square foot units sold in the prior year; 2) multiplied by 900 square feet; and 3) the affordable home sale price for a household earning Park City's workforce wage subtracted from the result.

- Questions: Is the City receiving adequate revenues from these fees such that the same number of units as the 15 percent residential or 20 percent commercial mitigation rate requirements could build? Has the City been able to use those funds to build the same number of units? Or is the in-lieu fee inadequate to build units in appropriate locations? Should it be based on assumptions that more accurately reflect the market? Looking ahead, are there even development opportunities for which the fees based on the same calculation will be useful? As a point of consideration, if land is becoming scarcer and its value continues to escalate, there may be a good justification for changing the fee methodology such that it results in a higher fee per unit.
- Approaches: There are a variety of approaches to structuring an in-lieu fee: 1) the difference between a market rate unit and a deed-restricted affordable unit; 2) a percent of the construction cost; 3) a percent of the maximum affordable sales price; 4) a percent of the land value to construct units elsewhere; and 5) nexus-based fee, which is described in recommendation above. There are a variety of considerations, however, that need to be made in selecting the appropriate fee: 1) is it sufficient to build a number of affordable units elsewhere equal to what would have been built; 2) is it sufficient to "buy-down" a similar number of units; and 3) how much does the City want to rely on outside information for the calculation?

  For example, the current methodology (basically #1 above) relies on one piece of outside information: the market rate price per square-foot from the Summit County Assessor. In #2 above, no outside information is needed for calculating a percent of the affordable sales price. In #3, outside information is required for two components: one for establishing a base construction cost per square foot that developers can agree is accurate, and another for escalating the value annually with the Bureau of Labor Statistics Producer Price Index (PPI), for example. In #4, outside data would need to be collected as well to document the value of land with comparable sales. In #5, the methodology would use outside data for the fee calculation, but because of its complexity of inputs, an annual escalation with the PPI, for example, might be too simplistic, while a full recalculation of the fee might be unnecessarily time-consuming.

4. ***The City should consider modifying the residential portion of the housing resolution to apply to all residential development.***

- The City should consider applying this portion of the resolution to all residential development. This is based on the review of the intent of the original housing resolution and the focus of subsequent iterations on annexations and MPDs, as well as analysis of historic building permit data, and an understanding of development in the pipeline. That is, it is unlikely that annexations or MPDs will be a majority or even a substantial component of development moving forward, such that the housing resolution as written will continue to be effective.
- For either of the previous options, EPS would recommend that an exemption be structured for projects that are contributing to the City's affordable housing inventory. As such, the exemption could be drawn at units that are priced below a certain affordability mark. For example, in 2014 the maximum affordable purchase price for a household earning 100 percent of median income ($89,886) was $359,600. Alternatively, the maximum affordable purchase price for a household earning 150 percent of the Park City workforce wage ($73,253 for a household of two persons) was $282,700. Whatever the threshold, EPS recommends that it serve equally as a proxy for the size of units being constructed.

- The implication of this is that all new residential development, large and small-scale projects of all structure sizes would apply. Given that the City has been concerned about recent increases in the number of larger single-family homes (i.e., second homes) that have not been subject to the resolution, it would be in the interest of the City to adopt a mechanism by which these are either subject to a higher mitigation, or that units priced more affordably (or of a smaller size) would be exempt.
- One option available is that the City could consider establishing a residential linkage program, which would establish the nexus between the level of affordable housing demand generated by units at various price points (i.e., proxy for size). There are two methodologies that such an analysis could employ: 1) other resort economies who have traditional residential linkage programs have conducted door-to-door surveys of the actual employment generated by their household (i.e., gardeners, housekeepers, other staff, etc.); and 2) there are a few larger, urban markets that have adopted residential linkage programs that rely on a nexus established on the basis of overall employment (i.e., jobs vis-à-vis household spending patterns). The first method requires primary data collection, and the send relies on input-output modeling factors.
- The other option is that the City keep its existing mitigation structure, but apply it to all new construction or demo-rebuild projects (i.e., no threshold). The fee in-lieu structure would be kept the same, but its outcome would require that smaller projects would be a fraction of a per-unit fee.

5. ***As for the debate over shared equity or ownership versus price appreciation limits, the City should consider a blended approach that focuses on shared equity and ownership.***
   - Both the shared equity and ownership structures lower the initial cost of home-ownership for households and offer them the opportunity to own the property in the long run while not necessarily attempting to manipulate the "value" of the property for the sake of keeping it in the affordable inventory. The limited appreciation model, on the other hand, seeks to manipulate the value by arbitrarily setting a price appreciation limit that is sometimes set to 2 or 3 percent. During high appreciation times, this is a frustrating element for buyers because they don't benefit from equity gains. Both of these approaches may offer the development community more flexibility in the product it builds, and may open up a slightly wider inventory of housing to households in need of affordable housing.
   - <u>Shared Equity</u>: This tool works well in an environment where considerable magnitudes of new housing are being built. Although it might have been very effective for Park City to have had this in place when a vast majority of new development was occurring in annexations and MPDs, there still are opportunities to use it moving forward. It would be worthwhile engaging city officials in a discussion of how to establish the program so that it could be utilized where effective. Specifically, the shared equity approach means that a borrower purchases a home by providing a downpayment, typically 5 percent, borrows approximately 75 percent of the value of the property and receives a low-interest equity loan of up to 20 percent (or some limit). At the end of the mortgage term or earlier, the equity loan is paid off in full plus 20 percent of the property's value escalation.

     In a housing market where construction costs are high, this may be an effective way to leverage the construction of units that would otherwise enter the market at slightly higher price points than the typical affordable unit. Because the mortgaged value of the property to the homeowner is actually 75 percent of its face value at the time of sale, it may also be a valuable technique to address the burgeoning need for middle-income housing, an issue that has been raised with increasing frequency. While a lower equity loan means less for a household to pay back over time, the larger the equity loan, the lower the "point of entry" for households in need. As such, the City may want to consider this element as a point of leverage to manipulate given market conditions. That is, the City could establish a policy where equity loans are available up to a maximum amount, and the borrower could choose whether or not to take advantage of the full value.

The challenge with this technique, however, will be that the City effectively cannot lend its credit or make loans. To take advantage of this option, the City will have to explore what third-party entities would be appropriate for administering such a program, such as Mountainlands Community Housing Trust or the Housing Authority. Perhaps the City could work to organize local and regional banks to establish a shared equity loan pool whereby the banks receive Community Reinvestment Act credits or other tax abatement incentives.

Beyond the obvious application for this structure on ownership condominiums, townhomes, and single-family homes, this may be a model worth exploring in a rental (or leasehold) context. Instead of an equity loan to the homebuyer, the City might explore whether it has the resources (i.e., pass through of capital funds) to grant lower interest equity loans to a new rental development in exchange for a portion of the units to be provided as affordable. While the specific terms of the stipulations would have to be worked out, this might be a second policy option to use for new rental developments (versus the option to utilize property tax abatements for new or rehabilitated rental properties). In such an example, instead of a 20 percent equity loan being paid off at the end of the mortgage term, the City receives a 20 percent share of the rents

- <u>Shared Ownership (Rent to Own) Approach</u>: This approach may be more valuable to a market like Park City that is mostly built out. This model is a subtle variation on the shared equity model, but it gives more flexibility to the City in making housing available at a wider range of price points. In some ways, this is a rent to own model. That is, a homebuyer could purchase a home with a mortgage commitment of somewhere between 25 and 75 percent, along with a 5 percent downpayment of the mortgaged value. The City or its agent would purchase the remaining share of the property. In addition to the mortgage payment, the homebuyer would pay "rent" to the City or the third-party entity to cover the debt service on that lower-interest mortgage. This model is particularly beneficial in an environment where borrowing costs are high (at the moment, that isn't necessarily the problem, but interests will likely rise in the future), and where the point of entry is high. This structure also allows homebuyers to enter a market they couldn't otherwise have entered and effectively rent to own. This means that homebuyers can increase their mortgage payments as their incomes rise.

6. *Define the timing of commercial and residential developments in the scheme of a revised and modified housing resolution.*

- It is important with the modification of existing policy or adoption of new policy that affects land development that a date be selected sometime in the future, at which point all applications received would apply to the revised policies. Depending on the length of time between, for example, permit application and time of construction or site plan and building permit, EPS recommends that, at the time City Council may approve the recommendations governing the housing resolution, a date be chosen that reflects this amount of time.

7. ***The City should expand the applicability of the density bonus for affordable housing and consider raising the density bonus.***

    - <u>Applicability</u>: The density bonus is granted only to MPDs in the City's Land Management Code. Using additional entitlements to motivate a developer to provider affordable housing can be a strong incentive in markets where additional density is particularly valuable. As a matter of policy coverage, EPS believes that the density bonus should be made available to any development that would look for ways to include affordable housing, including commercial and infill developments.
    - <u>10 percent density bonus</u>: The density bonus is frequently the strongest incentive an inclusionary zoning ordinance can offer in any setting where development pressures exceed entitlement. In EPS's experience, an increase in density, while greater efficiencies of land are usually realized (lowering the per-unit costs of land), is still associated with more construction costs. There are two challenges for most communities utilizing this incentive.

      On one hand is <u>calibrating the amount of density</u>, recognizing the marginal costs of construction, so that it has sufficient residual value to motivate a developer to pursue it. On the other hand is <u>calibrating the amount of the "requirement"</u> so that it doesn't eliminate the positive residual value of the density bonus itself. That is, there is value in the density bonus that can be leveraged for additional community benefit (i.e., affordable housing), but it needs to be of sufficient scale so as not to make the density bonus worth pursuing at all.

      Currently, Section 15-6-5(A)(1)(b) allows the Planning Commission to grant a maximum of 10 percent density bonus if a developer proposes an MPD where more than 30 percent of the equivalent units are affordable (or employee) housing. Therefore a developer of a residential MPD in Park City would have two basic choices: comply with the standard 15 percent set-aside requirement, or provide an additional 15 percent affordable housing for 10 percent additional density. It is very unlikely that these two elements have been calibrated such that a developer would be economically indifferent to the two choices – i.e., they would both yield the same financial return, or even ideally that the financial return of the project with the density bonus is actually higher.

      EPS recommends that the City re-evaluate its motivation for the two factors and discuss to what extent they can be brought into closer economic alignment. For example, a density bonus of 20 to 40 percent may be necessary (depending on the scale of the development and its construction type – wood frame, steel, or concrete) to offset the increased requirement for affordable housing.

8. ***The City should establish priorities for allocating the recent $40 million RDA Fund allocation.***

    - Previous Councils have drawn made important, symbolic, but necessary declarations of need, intent, and priorities in the housing resolution. The recent allocation of $40 million for capital is an important backdrop to such conversations. The City should engage its elected officials, however, in a policy discussion oriented around determining and voicing their concerns, vision, and direction regarding housing priorities.
    - That discussion should utilize major analytical findings from this study as guideposts for policy debate, not necessarily as prioritizations or exact magnitudes of need. The analytical findings of this study, and other studies that have preceded it, can be

interpreted as a selection of ways to look at this need. As there are multiple methodologies here and developed throughout the years by PCMC staff, there is a need to view these findings through the lens of political priority, perceived urgency, as well as within the context of other City priorities.

- EPS recommends that the City consider the various programmatic ways it might utilize the allocated funds. Programmatic considerations include making some portion of the funds available through a Notice of Funding Availability (NOFA), through which the City could create a competitive environment among both housing developers and service providers for use of the funds. Such a process can leverage the private sector for creative and financially efficient uses of funds.
- Another potential programmatic use of funds could be the acquisition of a strategic parcel of land that the City believes might be valuable in the future as a mixed-use redevelopment, in which the land could be leveraged for a public-private partnership development.
- In addition, some portion of the funds could be allocated to the purchase of existing units that might be appropriate for a shared equity or shared ownership program.
- While the City is not authorized under its accounting rules to make loans (i.e., for the purpose of establishing a mortgage pool or shared equity program), the City should still engage in discussion around who would be an appropriate entity to carry out such a function, how it would be done, and what variety of programs it would offer. It is valuable to consider that the original resolution (37-91) set forth an objective to establish a mortgage pool, working with lenders. While it is not clear from subsequent versions of the resolution whether this concept was ever piloted, it is clear that there are obvious obstacles to doing it today. Furthermore, it does not appear that the Mountainlands Community Housing Trust offers this type of assistance through its various ownership programs.
- In terms of beneficiaries, the City could utilize analysis of affordability conditions from this and other studies to identify magnitudes of need, looking at income level, community workforce contingent, and the type of development typically associated with that type of need. For example, EPS prepared revisions of previous gap analyses as well as a new methodology to estimate magnitude of housing type need by respective income levels of in-commuters.
- Based on the analysis of trends, the City would see more effective results and higher production if it focused more on community-based solutions, such as use of funding mechanism, than relied solely on its housing resolution, which is a development-based approach.