Affordable Housing
Exploring Two Important Types of Affordable Housing

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What is Affordable Housing?

The term "affordable housing" is often used in a more general way — for example — when people refer to affordable housing as a need, such as when someone says "we need more affordable housing" or "I wish I could find affordable housing in the Bay Area." The term is also used when local, state and federal governments refer to housing that is "affordable" – that is, when a household pays no more than 30 percent of its income towards rent and utilities (for renters) or mortgage and associated costs of homeownership (for homeowners), such as insurance, homeowner association dues, and taxes.

The latter definition is widely used by governments and recognizes that households have other essential expenses, including food, clothing, healthcare, childcare and transportation. The term can also refer to ***housing that is targeted to households with low or moderate incomes by covenants, agreements, laws or other enforceable mechanisms***. Such affordable housing includes:

- ***Subsidized Affordable Housing***, which refers to deed-restricted, affordable housing developments that have enforceable covenants covering income eligibility and rents or sales price, often because the developments received government subsidies. These subsidized projects include public housing, Tax Credit projects, Habitat homeownership units, and a few other varieties of assisted housing. Affordable housing developers, local governments, and housing advocates often use the term "affordable housing" to refer to these types of subsidized projects.

- ***Inclusionary Housing***, which is typically built by a market-rate developer without the help of government subsidies. Like subsidized affordable housing, affordable units in inclusionary developments are restricted to certain income groups – with restrictions placed on the rents or price levels – although such restrictions are often in effect for a shorter period of time than is the case with government subsidized projects. Many jurisdictions in the Bay Area and elsewhere have adopted Inclusionary Housing ordinances or programs.

Rent-controlled housing is another form of affordable housing, although rent-controlled units are not restricted to target only households at specific income levels. Instead, rent control ordinances place restrictions on rent increases and evictions. Beginning in 1999, however, state law in California allowed rents to be re-set to "market" levels when an existing tenant vacates and a new tenancy begins ("vacancy decontrol").

This brief fact sheet will explore two of the most common forms of affordable housing: inclusionary housing, and stand-alone, subsidized affordable housing.

**** First – A Word About Income Categories and Housing Need ****

By government definition, *"Moderate-Income" means a household with an income that is 120% of the "Area Median Income" (AMI), "Low-income" means a household with an income that is 80% of AMI, "Very-Low Income means a household with an income that is 50% of AMI, and "Extremely-Low Income" means a household with an income at 30% of AMI.* **In San Mateo County, the HUD-defined "Unadjusted Area Median Income" (AMI) for a family of four currently is $115,300.**

The chart below lists these income definitions and the amount of rent a family in San Mateo County can "afford" (i.e., that is no more than 30% of their household income):

U.S. Department of Housing & Urban Development (HUD) Defined Income Levels	**Percent of "Area Median Income" (AMI)**	**Household Income** (for a 4-person family in **San Mateo County**)	**Rent for a 2-Bedroom Unit** that equals 30% of the Household Income
"Moderate Income"	120% of AMI	$ 138,350	$ 3,459 *
"Low Income"	80% of AMI	$ 92,250	$ 2,306 *
"Very Low Income"	50% of AMI	$ 57,650	$ 1,481 **
"Extremely-Low Income"	30% of AMI	$ 34,600	$ 888 **

* Not set by HUD. Calculated as 30% of the Household Income for 80% or 120% of AMI, divided by 12.

** Rent limits set by HUD for HUD programs (Tax Credit-allowed maximum rents are slightly different)

Those with the lowest incomes have the most difficulty finding and keeping a place to live in the Bay Area and in other high-cost areas. Data from sources including the most recent U.S. Census Bureau, 2011-2015 American Community Survey 5-Year Estimate indicates that the need in San Mateo County for affordable rental homes for lower-income workers, seniors and others far outstrips the supply: for example, there are over 32,000 extremely-low and very-low income renter households in the county, but less than 10,000 rental units in the county that are affordable and available for these households – leaving a supply gap of more than 22,000 rental homes for those earning up to 50% of Median Income. The supply of affordably priced housing also falls far short of the need for thousands of other low and moderate-income households in the county.

Inclusionary Housing

What Exactly is Inclusionary Housing?

Many cities and counties have adopted inclusionary ordinances designed to help them meet their affordable housing needs as shown in their respective housing elements. These ordinances require developers to include a certain number of affordable units in their projects, or pay an in-lieu fee. To offset the cost of the inclusionary units, a city or county program lets developers build bigger or taller residential buildings – and sometimes gives them other financial incentives – to help develop some of the units as affordable housing. Often called "Below Market Rate", "BMR," "Inclusionary Housing" or "Inclusionary Zoning," these programs require developers to sell or rent some of their units in new developments at a below-market-rate price or rent level that is affordable to lower or moderate- income households.

In summary, inclusionary zoning requires developers to build affordable housing but gives builders some incentives in exchange for creating the affordable housing.

How Does Inclusionary Housing Work?

Typically, the inclusionary units are mixed in with other units throughout the building. But some jurisdictions allow the developer to meet the inclusionary requirements by partnering with a non-profit or for-profit affordable housing developer to build a "stand-alone" 100% affordable housing complex, either on-site or on another nearby site. Such "stand-alone" affordable housing projects created in response to an inclusionary requirement can be financed the same way other subsidized affordable housing projects are financed but usually include a substantial developer subsidy in the form of a land contribution, the preparation of the site for development and/or a substantial financial contribution to the project. And as will be explained below, such stand-alone affordable housing developments have some distinct advantages compared to projects with inclusionary units that are mixed together with market-rate units.

First, let's consider inclusionary housing that is built as part of a market-rate housing development. In this case, developers typically get a density bonus, which allows them to build more units than normally allowed in that zone if they meet a requirement to set aside a certain percentage (typically 15% - 20%) of the units for affordable housing. In such instances, the developer can only discount the rents on the inclusionary units by a certain amount and still keep the whole development financially workable. That is the reason inclusionary housing projects typically target their inclusionary units for **moderate-income** families, or a combination of some Moderate-income families and some Low-income families.

If a project were required to set aside 15% or 20% of the overall units as Very-Low or Extremely-Low Income units, the rents generated from the inclusionary units would be so minimal that the whole development could be rendered financially infeasible. Cities often like inclusionary housing because it guarantees the affordable units are created as part of the development.

Stand-Alone Subsidized Affordable Housing

Some Reasons for Stand-Alone Subsidized Affordable Housing

As noted at the beginning of this article, inclusionary units provided within a market-rate development typically have their rents set at a level that can be afforded by moderate income families or a combination of some "moderate-income" and some "low-income" families. This absolutely provides a benefit to these families and a social benefit to the entire community. However, many housing advocates prefer that developers contribute land, partner with affordable housing developers, or pay in-lieu housing fees because this allows the public and affordable housing sector to leverage the developer's contribution to create a greater number of units at a deeper affordability level than would be created through the provision of inclusionary units.

Households with the greatest challenges finding decent, safe and affordable housing are those at the lower end of the income spectrum – those at or below 50% of the Area Median Income – who are classified as "Very Low Income" and Extremely Low Income". **Many military Veterans, working families, and seniors on fixed incomes, for**

example, fall into these income categories. Some individuals also need various supportive services to be able to live successful and independent lives. Providing subsidized housing with supportive services for these families and individuals is also a very important individual and community benefit.

All multifamily developments — whether market-rate or affordable — are expensive to build, especially in the Bay Area. However, as illustrated in the table below, the way deeply income targeted, subsidized "stand alone" affordable housing gets financed and produced is *very different* from how inclusionary housing is financed and produced. First, this type of stand-alone affordable housing development is produced by experienced affordable housing developers who are adept at securing all types of financing for the project.

Second, because tenant rents in affordable rental housing developments are kept at low levels, the amount of total rents that can be generated is limited, and will only support a relatively small construction-period loan followed by a small permanent mortgage loan. As illustrated in the table below, **the rest of the cost of building the development** must be supported by a combination of sources -- private investors who receive a tax credit for contributing equity (commonly referred to as "tax credit financing"); local, state and federal government subsidies; land donation; fee reductions and waivers; and other cost-saving incentives and special financing tools.

Without such multiple "layers" of financing assistance, stand-alone subsidized affordable housing serving lower income seniors, families and individuals could never get built.

Third, only stand-alone affordable rental housing has the structure and ability to support resident services such as after-school tutoring programs, health and nutrition classes, job training skills, etc. Finally, only this type of affordable housing can generate the resources to serve very low-income community members with special needs, such as chronically homeless persons, frail elderly, or persons with serious physical or mental health challenges.

How Does the Financing for Stand-Alone Affordable Housing Work?

Putting together the financing for an affordable housing project is sort of like making a 7-layer cake. It is very complicated and often takes two to three years to accomplish. The illustration below shows how a typical affordable rental housing project might get all the financing it needs:

Layers in the Affordable Housing "7-Layer Cake"	
FINANCING SOURCE	**PERCENTAGE OF TOTAL DEVELOPMENT COSTS**
Equity: Tax Credit Equity	Approximately **40%**
Local, State & Federal Subsidies:	Approximately **40%**
- City/ County / Public agency land donation	
- City/ County/ State/ Federal subsidies such as Measure K funds, funds generated by City impact or in-lieu fees, CDBG or HOME funds, Sec. 8 Project-Based assistance, etc.	
- Fee waivers / reductions	
- Other cost-reduction incentives such as Parking reductions, density bonus, etc.	
Debt: Perm Mortgage supported by the Rents	Approximately **20%**

In Conclusion

For San Mateo County — as well as the greater Bay Area region — there is a growing need for all types of affordable housing. Cities can take concrete steps to encourage the creation of inclusionary *and* stand-alone subsidized affordable housing -- two of the most important types of long-term affordable housing that can accommodate households with a range of incomes and needs. Each of these strategies for creating affordable housing has particular advantages and benefits, but together they can help fill the supply gap for housing that is affordable to working families, seniors, veterans, individuals with disabilities, and many others in need of safe, decent, and affordable housing.