SPUR
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February 22, 2016

San Francisco Board of Supervisors
1 Dr. Carlton B. Goodlett Place, Room 244
San Francisco, CA 94102

Re: Changes to San Francisco's inclusionary housing requirements

Dear Supervisors:

I am writing to express grave concern about some potential changes to San Francisco's inclusionary housing law.

SPUR has been deeply involved with inclusionary housing since the mid-1990s, and helped develop the original ordinance. We believe that inclusionary housing can be an important tool for generating below-market rate housing.

However, it is a tool that can backfire if it is not done right, by reducing the overall amount of housing produced in the city – paradoxically leading to higher housing costs for most people. This is not a question of ideology; it is a question of math. For an inclusionary housing law to work as a way to reduce overall housing costs, the numbers need to be set at a level that makes it viable to produce a large amount of un-subsidized housing.

Based on our review of development pro formas, we do not believe the proposed 25% is workable as a baseline requirement, although there will certainly be special situations where it is workable.

It is often pointed out that inclusionary housing, along with other development fees and exactions, comes out of the land price, because developers are forced to bid reduced amounts for the parcels they purchase. In the long run, we agree with this general assessment. So long as the requirements are known in advance, and the rules don't change after developers enter into options for land, the costs of exactions and fees can be factored into the prices bid for the land.

However, what follows from this analysis is that the great risk of inclusionary housing policies, like other development fees and exactions, is of reducing the amount of land that is put into development, thereby reducing the overall supply of housing. Land has other potential uses in a city, and developers must be able to pay a premium above what the existing uses can pay or landowners will simply not sell.

There has been no analysis, to date, of the impacts of the increased inclusionary requirement on land availability for residential development.

Proposition C of 2012 made two changes to the Charter: it created a budget set-aside to fund housing subsidies each year; and it put in a cap on the overall level of inclusionary housing. Both changes were conceived of as a "bargain" that would shift the funding of affordable housing away from development exactions and onto the broader tax base of the city. The idea was to create a permanent stream of funding for affordable housing while also creating certainty that the inclusionary requirement would be set at a feasible level – a way to ensure that the city maximized the production of both subsidized and un-subsidized housing. If the Supervisors wish to un-do this bargain, so be it. But the new process should institute an inclusionary housing program that does two key things:

1. **Establish a "grand-fathering" date for projects already in the pipeline**. The intent should be to allow projects that have already made land deals to go forward under the rules in place at the time of their purchase. We suggest that any projects that have submitted environmental applications prior to the date on which inclusionary housing requirements (or other fees or exactions) change, should be protected from changes that increase their cost structure. By the time an environmental evaluation application is filed, developers have made significant investment in a project by purchasing land or entering into option agreements and have solidified many of their decisions about a deal structure and the overall project.
2. **Establish a process for changing inclusionary housing requirements based on analysis of the financial feasibility.** The initial legislation that created the city's inclusionary requirement in 2002 relied on just such a process. It is fine to assume that added costs will flow through to reduced land prices in the long run, but we cannot blithely assume that any cost can be passed on to land owners without understanding the sensitivity in land prices and the potential impacts of suppressing housing supply.

We would urge you to adopt these changes to any reforms of the city's inclusionary housing laws.

Sincerely,

Gabriel Metcalf
President & CEO, SPUR