City of Fort Bragg

Inclusionary Housing In-Lieu Fee Nexus Study

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Background

Inclusionary housing is used by over 170 cities and counties in California to require affordable units for low- and moderate-income households in new market-rate residential projects. Inclusionary housing regulations help achieve the following policy goals: 1) development of more affordable housing units; 2) integration of affordable units with market rate units in mixed-income projects; 3) and, due to required state incentives and state density bonus law, inclusionary housing regulations typically result in more market-rate units than is permissible with existing regulations.

Local communities are required by state law "to provide alternative means of compliance (with the inclusionary housing requirement) that may include, but are not limited to, in-lieu fees, land dedication, off-site construction, or acquisition and rehabilitation of existing units." The City of Fort Bragg has adopted all of these alternative means of compliance. The City's Fee Schedule requires that the City determine the inclusionary fee at the time of application. The City recently received an application for a 53-unit market rate rental project, and this analysis provides a rational basis for the City to set its inclusionary housing in-lieu fee.

Inclusionary Housing fees are typically adopted per unit or per SF. This analysis recommends the /SF methodology as it is more responsive to the actual unit size in a project. In other words, with a per SF approach, projects with more small units would pay a proportionally lower fee than a project that includes fewer larger units. With a per unit fee approach the reverse would be true. As the City Council has set a policy goal of increasing housing stock, the /SF in lieu fee approach is preferable as it incentives more smaller units.

Introduction & Methodology

The City should adopt two inclusionary housing in-lieu fees, one for rentals and one for for-sale units, as the cost of producing single family detached for sale units is more than the cost of providing attached rental units and the method for calculating the in-lieu fee is likewise different due to data constraints and different inclusionary housing requirements for rentals versus for sale units.

Rental Methodology. The inclusionary housing fee for rental units is calculated from the net present value of the difference between the required affordable rent and the market rate rent over the required 45-year period of affordability. As there have been no large-scale market rate apartment projects constructed within Fort Bragg in the past 20 years, it is not feasible to obtain per square foot construction cost estimates for such a project, and it is therefore not possible to complete an analysis of the different in cost between producing a market rate and an inclusionary housing unit. Additionally, the net present value methodology more accurately captures the true cost of providing an inclusionary housing unit to the developer.

For Sale Methodology. For "for-sale" inclusionary units, the in-lieu fee amount should be based on the gap between the amount that a low-income household can afford to pay for a mortgage and the market-rate cost to produce that unit. For example, if it costs $450,000 to produce a modest home but lower income households can only afford a mortgage of $275,000, then the in-lieu fee would be $75,000/inclusionary unit or $9.38/SF/for all development to cover the difference (e.g. the affordability gap).

Rental Housing In-Lieu Fee Analysis

Market Rents. To determine the market rate rent, MJC analyzed current rental rates on craigslist for Fort Bragg by unit size. As noted in Table 1, the average monthly rent is $1,324/month for a 1-bedroom and $1,838/month for a 2 bedroom. This analysis used an average of both the one and two bedroom rents because the census does not provide median household income by household size for Fort Bragg and so it is not possible to prepare an analysis with a more fine grained approach that would calculate AMI for a family of 4 for two bedroom units and AMI for a family of 2 for a 1-bedroom unit. In Fort Bragg the current average market rent is $1,581/month/unit, which is used in this In-Lieu Fee analysis.

Table 1 - Market Rate Rentals, Ocober 2024

Name	# of bedrooms	amount
Studio Apt	0	$ 1,295
Newly remodeled studio	0	$ 1,200
Studio Apartment	0	$ 1,295
		$ 1,263
Cottage in the redwoods	1	$ 1,500
Harbor Life	1	$ 1,400
Harbor Living	1	$ 1,600
One Bedroom Apartment	1	$ 1,090
Redwood Cottage	1	$ 975
Downtown	1	$ 1,300
I bedoom Lower Floor	1	$ 1,400
		$ 1,324
Now accepting Applications	2	$ 1,063
Downstairs	2	$ 1,600
Large 2 Bedroom	2	$ 2,850
		$ 1,838
Average of 1 and 2 bedrooms		**$ 1,581**
Shewrood Duplex	3	$ 2,300
3BR/2BA/Ocean View	3	$ 2,500
		$ 2,400

Source: MJC,2024; Craigslist Apts for rent

Rental Inclusionary In-Lieu Fee Calculation

Table 2 below calculates the maximum inclusionary housing fee for each income category in the Inclusionary Housing Ordinance as follows:

- Maximum annual income for each affordability level for rental housing is defined as a percentage of Area Medium Income. Per the City's ordinance, one third of inclusionary units must be affordable to low-income households (less than 50% AMI) one third must be affordable to households of moderate-income (100% of AMI) and one third for workforce housing (120% of AMI).

- The annual income limit for households at each income level (low, moderate, workforce).
- Maximum rent that a household can afford at the relevant income level. This is set at 30% of annual income per HCD requirements.
- The monthly rent reduction, which is market rent minus the calculated affordable rent.
- The amortization of the monthly rent reduction over 45 years which is divided by 1,100 SF to arrive at a maximum inclusion fee on a per square foot basis. The per square foot cost is then multiplied by 15% (as the ordinance requires that 15% of all project units be affordable. This final number is the cost per square foot of inclusionary housing for the entire project (in SF).

Table 2 below illustrates the net present value of the rental income reduction for each category of affordable units. As noted in the table the "opportunity cost" to the developer of providing the inclusionary units would be $21/SF for the entire housing project. In other words, if a developer did not have to dedicate 15% of units to affordable housing, they would earn $21/SF more over the life of the project. This fee rate would amount to $1.2 million in inclusionary housing in-lieu fees for the proposed project for 1151 S Main Street.

Table 2: Multi-Family Rental Inclusionary Housing Fee Calculation, 45 years of affordability

	Annual Income Limit	Monthly Affordable Rent (30% of gross income)	Market Rent (Average of 1 & 2 Bedrooms)	Monthly Rent Reduction	Net Present Value of 45 years of Reduced Rental Income	Max In-Lieu Fee Cost/SF
Inclusionary Units 50% of AMI	$ 31,062	$ 777	$ 1,581	$ 804	$ 65,131	$ 59.21
Inclusionary Units 80% of AMI	$ 49,698	$ 1,242	$ 1,581	$ 338	$ 27,391	$ 24.90
Inclusionary Units 120% of AMI	$ 74,548	$ 1,864	$ 1,581	$ (283)	$ (22,929)	$ (20.84)
Average					**$ 23,198**	**$ 21.09**

Notes:
Median Household Income in 2022 was $57,662, American Community Survey, US Census
Inflation adjusted Median Household Income in 2024 was $62,123

The City of Fort Bragg's maximum in-lieu fee is high because the ordinance requires 45 years of affordability. The City's inclusionary housing ordinance was adopted when redevelopment agencies and tax increment financing were available as tools to encourage affordable housing. Per State statute at that time, all housing projects assisted with redevelopment funds had to achieve 45 years of affordability. The inclusionary ordinance was designed to match that term of affordability per the recommendation of the consultant. However, redevelopment was abolished by Governor Brown in 2011 to help solve the State's recession-induced budget deficit. Fort Bragg's ordinance was not revised (because case law had invalidated the ordinance) and the City's 45 years of required affordability is much longer than most other agencies.

However, the City is not required to impose the maximum permissible in-lieu fee. On the contrary, jurisdictions typically adopt fee amounts that are substantially less than the total amount justified by the strict nexus analysis. Accordingly, the table below includes the same analysis but with 25 years of required affordability. With 25 years of required affordability, the inclusionary housing in-lieu fee would fall to $11.72/SF for the entire housing project. This would amount to $691,000 in inclusionary housing fees for the proposed project at 1151 S. Main Street.

Table 3: Multi-Family Rental Inclusionary Housing Fee Calculation, 25 years of affordability

	Annual Income Limit	Monthly Inclusionary Rent (30% of gross income)	Market Rent (Average of 1 & 2 Bedrooms)	Monthly Rent Reduction	Net Present Value of 25 years of Reduced Rental Income	Max In-Lieu Fee Cost/SF
Inclusionary Units 50% of AMI	$ 31,062	$ 777	$ 1,581	$ 804	$ 36,184	$ 32.89
Inclusionary Units 80% of AMI	$ 49,698	$ 1,242	$ 1,581	$ 338	$ 15,217	$ 13.83
Inclusionary Units 120% of AMI	$ 74,548	$ 1,864	$ 1,581	$ (283)	$ (12,738)	$ (11.58)
Average					$ 12,888	**$ 11.72**
Notes:						
Median Household Income in 2022 was $57,662, American Community Survey, US Census						
Inflation adjusted Median Household Income in 2024 was $62,123						

Rental In-Lieu Fee Recommendation. MJC recommends an inclusionary housing in-lieu fee for rentals of between $4/SF and $8/SF. This fee is sufficiently low to allow a smaller project, that can't accommodate affordable units on the project site, to buy out of the requirement and proceed with the development of market rate units. Most larger projects will receive sufficient financial benefits from the density bonus and the planning incentives (required by state law and the City's ordinance for the construction of inclusionary housing) to build the units rather than pay the fee.

For Sale Housing Analysis

Production Costs

The cost to produce a typical unit of for-sale housing in Fort Bragg will vary depending on the size of the unit and if it is attached as part of a condominium or detached in a single-family home subdivision. Housing costs will also vary with the home's location, type, level of finish etc. MJC has developed a basic housing production cost/SF based on data provided by local contractors.

The cost estimate assumes a "basic" unit size of 1,100 SF with basic finishes and site infrastructure costs on a typical lot in Fort Bragg. The production cost for a single-family unit range from $375 to $450 per square foot, while the production cost for multi-family units is not available locally because no recent market rate multi-family projects have been built.

This analysis, therefore, assumes a $425/SF housing development cost, which includes the cost of construction, design, permitting and fees. It does not include the cost of land.

For Sale Inclusionary In-Lieu Fee Calculation

The table below calculated the maximum inclusionary housing fee for each income category in the Inclusionary Housing Ordinance as follows:

- Maximum annual income for each affordability level for "for Sale" housing is defined as a percentage of Area Medium Income. Per the City's ordinance, one half of inclusionary units must be affordable for households of moderate income (100% of AMI) and one half for workforce housing (120% of AMI).
- The annual income of households at both income levels.
- The maximum amount of mortgage for each household could qualify at each income level, assuming 10% down payment.
- The cost gap, which is the actual cost to construct minus the mortgage that a household could qualify for.
- The resulting inclusionary housing fee which is the cost gap divided by 1,100 SF to get a per square foot cost and that number multiplied by 15% (the affordably housing requirement) to arrive at a cost per square foot for the entire project.

As illustrated in the table below, the maximum inclusionary housing in lieu fee for "for sale" units would be approximately $28/SF calculated over all the units in the project.

Table 5: Financing Gap and Inclusionary Fee, "For Sale" Units

Maximum Income Level for Affordability Requirement	Income Level	Mortgage Qualification Amount	Unit Cost	Cost Gap	Inclusionary Fee/SF
Moderate Income - 100% of AMI	$ 62,123	$ 239,800	$467,500	$227,700	$ 31.05
Workforce Housing - 120% of AMI	$ 74,548	$ 282,700	$467,500	$184,800	$ 25.20
Average				**$206,250**	**$ 28.13**
Source: MJC 2024					

For Sale In-Lieu Fee Recommendation. MJC recommends an inclusionary housing in-lieu fee for "for sale units" of between $10/SF and $15/SF. This fee is sufficiently low to allow a smaller project, that can't accommodate affordable units on the project site, to buy out of the requirement and proceed with the development of market rate units. Most larger "for sale" projects will likely pursue one of the other alternative equivalent actions such as providing second units or donating land to a non-profit developer. Incentives and density bonuses are generally not compatible with the market for single family homes.

Comparable In-Lieu Fees

Table 6 illustrates inclusionary housing fees from other cities and counties in Northern California. Clearly from a review of the table the amount of the inclusionary housing in-lieu fee varies widely across jurisdictions depending on housing costs, area medium income, rental rates and policy goals. This comparison does not provide "an answer" as to what the City should charge for the in-lieu fee; it only provides a comparable range. Ironically, Mendocino County is the extreme outlier in terms of the amount of the in-lieu fee. Their fee was adopted in 2009 and is likely neither supported by a nexus study nor enforceable.

Table 6: Comparison of Inclusionary Housing In-Lieu Fees for Northern California

Jurisdiction		Amount/SF
Placer County	$	2.59
Sonoma County	$	4.96
Mendocino County	$	75.11
Marin	$	5.00
Average	**$**	**21.92**
Healdsburg	$	16.67
Windsor	$	4.44
Santa Rosa	$	10.00
Walnut Creek	$	25.76
Average	$	14.22

Source: MJC 2024, each city's webiste

Conclusion

When deciding if they will pay an in-lieu fee or provide required inclusionary units, a developer will weigh the relative monetary value of the benefits of the density bonus and planning incentives, which are required by law if they provide the inclusionary housing units, versus the direct cost of paying the in-lieu fee.

The inclusionary housing requirement can result in more affordable and market rate units and improve the financial performance of a housing project, when the approved planning incentives and density bonus are of sufficient benefit to offset the marginal cost of providing the inclusionary units.