Housing Policies in Appreciating Markets: Perspectives from the Development Community in the City of Chicago

Technical Assistance Panel

Co-Sponsored by

Campaign for Sensible Growth
ULI Chicago

The Urban Land Institute (ULI) is a national, nonprofit education and research institute that is supported by its members. Its mission is to provide responsible leadership in the use of land in order to enhance the total environment.

The Chicago District Council consists of more than 800 ULI members living and working in the Chicago Region. One of the first ULI District Councils formed, today it is one of the largest in the nation. The Chicago District Council presents annual lifetime achievement awards, holds monthly leadership breakfast meetings and leads periodic advisory workshop panels for local governments. The Public Policy Committee, formed in early 2002, oversees technical assistance for the Chicago District Council.

Campaign for Sensible Growth

The Campaign for Sensible Growth is a coalition of government, civic and business groups. The Campaign promotes strategies to enhance the economic vitality of the six-county Chicago region while preserving open space, minimizing the need for costly new infrastructure and improving livability of our communities. Among the goals of the Campaign is the revitalization of existing communities. The ULI Chicago District Council was an original Steering Committee member of the Campaign for Sensible Growth and has partnered with the Campaign for the past four years on symposiums and forums exploring matters of joint interest.

Funders of the Campaign for Sensible Growth:

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Housing Policies in Appreciating Markets is the first in a series of Technical Assistance Panels convened by the Urban Land Institute Chicago and Campaign for Sensible Growth. The 2002 series of panels also focused on Richmond, Ill. (Chicago) and Highwood, Ill.

For more information on the series visit www.growingsensibly.org or call 312/922-5616.

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The Chicago housing market is the strongest that it has been in decades. Moving beyond the traditional upscale areas of the Gold Coast and Lincoln Park, the 1990s saw dramatic increases in both housing production and market value in many neighborhoods, particularly along the lakefront and in relative proximity to downtown jobs on the Near South, West and Northwest sides. However, escalating markets can impact both existing homeowners and renters. While homeowners may benefit financially, renters are often priced out of the neighborhood.

On May 16, 2002, 12 leading professionals from the Chicago real estate and development community spent a day hearing from local and national experts about inclusionary housing policies, and how different programs might impact the city. Inclusionary housing refers to programs or policies that either provide incentives for or require affordable housing as a component of a private, market-rate development. The workshop was convened by the Urban Land Institute Chicago and Campaign for Sensible Growth in response to questions posed by the City of Chicago.

The findings contained in this report are solely the opinions of the panel. The report is advisory in nature and will require further consideration by public officials and stakeholders concerned with these issues.
Workshop Participants

Twelve participants from the development community were recruited to volunteer their time to review an extensive briefing book in advance of the workshop and spend one full day deliberating as a team. The participants chosen are leaders in their fields – for-profit and nonprofit developers, finance experts, real estate lawyers, and market analysts. In addition, Edith Netter, a national expert on inclusionary housing, provided a detailed presentation. The panel also heard presentations on an existing voluntary set-aside program from a local developer and representatives from the City of Chicago Department of Housing (DOH).

Chair: Mary White Vasys, President, Vasys Consulting Ltd.

Rolando Acosta, Attorney, Acosta, Kruse, Raines & Zemenides
Dan Burke, Vice President - Development, Chicago Community Development Corporation
Robin Coffey, Vice President of CRA Expenses, Harris Bank
Philip Darrow, Vice President, Eastern Regional Counsel, Del Webb Communities of Illinois
Allison Davis, President, The Davis Group
Bruce Gottschall, Executive Director, Neighborhood Housing Services
Richard Klawiter, Partner, Piper Rudnick
John McLinden, Partner, Centrum Properties
Robert Miller, Senior Vice President, Applied Real Estate Analysis, Inc.
Raul Raymundo, Executive Director, The Resurrection Project
Penny Wallingford, Project Coordinator, The Shaw Company
Terry Young, Director, Chicago Partnership Office, Fannie Mae

City of Chicago Representatives: Commissioner Jack Markowski, Eduardo Camacho, Stacie Young and Kelly Clarke (Department of Housing), and Tom Smith (Department of Planning and Development).

Planning Group: Scott Goldstein (ULI and Metropolitan Planning Council), Doug Porter (ULI), Don Shindler (ULI and Piper Rudnick) and Ellen Shubart (Campaign for Sensible Growth).
Context for Workshop Discussion

The U.S. Census shows that Chicago’s population increased by 36,754 from 1990 to 1999 – the first increase since 1950. Increased housing development has been fueled by escalating prices, especially in some areas of the city. As a result of higher prices for both for-sale and rental units, the workshop looked at ways to address affordable housing needs of community residents, while taking advantage of the strong development market. The workshop based its work on several key trends and values:

- Certain areas of the city are experiencing dramatic change.
- Strong development activity is occurring.
- Land values and housing prices are increasing at a rapid rate.
- Residents and public officials want new investment in their communities and to maintain affordability.
- Appreciating land values and housing prices can impede new development of affordable housing.
- Market-driven reinvestment is important for healthy communities.
- Any inclusionary housing program should be formulated with the goal of long-term affordability.
- Inclusionary housing programs are most effective for “workforce housing” needs for households with incomes between 60 percent and 120 percent of area median income.
- Chicago currently has a voluntary inclusionary housing program (CPAN), with approximately 150 units in the development pipeline.
- Inclusionary housing programs can be mandatory or incentive-based.
- Incentive-based programs can require inclusion or offer an option in exchange for incentives.
- Incentives can include density bonuses, zoning change approvals, expedited permit review processes, and waivers of fees or other requirements.

Questions Posed to Participants

Seven questions were posed to the workshop. After hearing presentations and asking questions during the morning, the panel convened privately over lunch and throughout the afternoon in two teams to develop answers to the questions. The panel as a whole then discussed the results of the team discussions and agreed upon a common set of answers to the questions.
Is the real estate market strong enough to support an inclusionary housing program?

- Some market areas in Chicago can support an inclusionary housing program, particularly on for-sale housing projects.
- Some areas of the city are not strong enough to support inclusionary housing policies. There are still many areas that need economic reinvestment and have an existing concentration of affordable housing.
- Implementation of inclusionary housing strategies should be targeted to specific areas based on market characteristics. These “target areas” can be defined by market and demographic characteristics. Triggers will need to be defined to determine which areas of the city should be eligible. Characteristics may include market activity, escalation of housing prices and the gap between current residents’ incomes and rising prices of real estate.
- Any program implemented should be flexible to respond to changing market conditions.
- It will be difficult to implement inclusionary housing strategies on market-rate rental development because so few rental development units are being developed. Rental housing development in Chicago is dampened by Cook County property tax policies that penalize apartment building owners and renters. Recent reforms to phase-in a reduction of Class 3 multi-family housing assessment levels (from 33 percent to 26 percent of market value) is a first step, but is being overshadowed by large assessment increases due to recent sales.
  - The minimum affordable housing set-aside in Class 9 affordable housing property tax incentive should be lowered from 35 percent to the level that would be used in an inclusionary housing set-aside program. For example, if Chicago’s inclusionary program requires 20 percent set asides, than the Class 9 program should be lowered to the same level so that city and county programs are coordinated and the maximum number of affordable units are developed.

How should target areas be determined?

- Recommend city-wide policies with standard criteria.
  - Designation at option of local neighborhoods with support of the alderman.
• There are different types of markets:
  • “Hot” markets have rapidly appreciating land and housing values and are losing their existing affordable housing. They are experiencing the fastest rate of change, especially when measured by land prices. The gap is growing fastest between existing residents’ incomes and the ability to pay for new units being developed.
  • “Warm” markets often adjoin “hot” markets, but property values are still low, thereby providing more opportunity for new affordable housing.
  • “Mature” markets are built out and generally high priced.
  • “Under-invested” markets need more private investment. Inclusionary housing policies that require set asides would clearly dampen new investment. Traditional affordable housing tools should continue to be used to improve the quality and availability of units in these areas – from New Homes for Chicago to tax credit programs. These areas may change to “warm” or “hot” over time.

• Start with “hot” markets first.
• Additional criteria could address rapidity of change and interest of local residents to retain or expand affordable housing.
• Local political support should be required.

**What would be the impact on overall development activity?**

• Impact will depend on the scope and nature of policies.
• Too many restrictions could discourage investment.
• Do not impose inclusionary housing requirements on commercial developments in Chicago (which is often called a “linkage” program). The commercial development market has not been strong, even during the robust 1990s. Commercial properties are already assessed for property taxes at over twice the rate of homeowners within Cook County and are effectively taxed at two to three times the rate of similar properties in all other parts of the Chicago region. This creates a competitive disadvantage to bring needed jobs into the city.
Should the program apply to all developments?

- Use incentive-based policies for all residential developments in target areas (new construction, condominiums, owner-occupied units, rental units and single-family housing).
  - Apply policies uniformly.
  - Deploy incentives quickly.
  - Be flexible to recognize specific project attributes.
- There should be no minimum size threshold. Instead, because single-family and small projects often attract higher income levels in many gentrifying areas and contribute to the price escalation in the market, small projects should be allowed the option of paying a fee.
- The difference between market sales price (or market rent) and affordable price or rent is the financing gap that must be covered by incentives or other public funding assistance.
- For condominium projects, pay particular attention to monthly assessments and building amenities to be sure long-term affordability is maintained.

Should fees be allowed in lieu of housing units on site?

- Yes, fees should be allowed, especially for:
  - small projects in target areas; and
  - high-priced developments in non-target areas.
- Fee options for high-priced developments allows for increased production of units in projects where costs are lower.
- Make fees high enough to support construction of new units. Fees should be based on costs of developing the units on site, thus resulting in a greater number of units if off-site construction is less expensive.
- Should not be used as inexpensive way to avoid production of new affordable housing.
- Could be structured on sliding scale to recognize the strength of the incentives offered and differing costs among sites and neighborhoods.

What percentage of units should be set aside for affordable units?

- From 10 to 20 percent of new units in target areas based on market conditions.
• Consider using a lower figure as an incentive for on-site units versus fees.
• For market-rate developments, base the percentage of affordable units in building on amount of incentives made available.

Who should be eligible for affordable units?

• Base sales price (or rental rate) should be based on household incomes of residents the City wants to target.
  • Between 60 percent and 120 percent of area median income households should be eligible.
  • Lower than 60 percent of median income is unlikely to be feasible due to development and, therefore, incentive costs.
  • Could be determined by average salaries of certain jobs (police officer, teacher) as a way to market the program.
  • Could be tied to length of residency in target neighborhoods (such as certain property tax incentive programs).
• Make sure counseling and other support services are available for new residents, such as those already offered by DOH and nonprofits.

Additional Considerations

• Resale restrictions are important to maintain affordability, but should also allow limited appreciation to homeowner.
  • Could tie formula to income level of homeowner.
  • Should remain affordable in perpetuity rather than be time limited.
• Oversight entity is needed to monitor program and adjust requirements and incentives over time.
  • DOH is the logical choice for this role.
• Inclusionary housing fees should go into a segregated fund to support affordable housing.

New Funding Ideas for Affordable Housing

• Generate new revenue by increasing state and/or local real estate transfer taxes.
• Raise zoning fees (i.e., for planned development applications).
• Invest city pension funds in affordable housing.
• Leverage individual development accounts (IDAs) to provide incentive for households to save for housing investments.

Summary of Developers’ Perspective

• Market can support a targeted inclusionary housing program in certain areas of the city.
• Inclusionary housing policies alone will not produce large amounts of affordable housing.
• Any program should be based on market realities.
• Any program should respond to changing market conditions over time.
• Any program should be applied consistently.
• Incentives should match the incremental costs of benefits attained.
• Reducing time delays in development approvals would be a strong incentive for more affordable housing.
• Relaxing certain development exactions (City requirements on development in order to gain zoning and/or permit approval) would be an incentive for more affordable units.
Special Thanks and More Information

ULI Chicago and the Campaign for Sensible Growth would especially like to thank Mary White Vasys, president, Vasys Consulting, Ltd. and City of Chicago Housing Commissioner Jack Markowski for their support, time and commitment to this project.

More information on these issues and the technical advisory program of ULI Chicago and the Campaign for Sensible Growth is available at www.ulichicago.org and www.growingsensibly.org.