



CITY OF CAMBRIDGE

Community Development Department

To: Planning Board
From: Community Development Department (CDD) Staff
Date: September 6, 2022
Re: **Incentive Zoning Rate Increase Zoning Petition**

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Petition Overview

Petitioner: City Council
Zoning Articles: 11.000 (Special Regulations)
Petition Summary: To amend Article 11.000 of the Zoning Ordinance by substitution with the following text: "(b) Housing Contribution Rate. The Housing Contribution Rate effective upon ordination shall be thirty-three dollars and thirty-four cents (\$33.34) per square foot of Gross Floor Area devoted to the uses that qualify the new development as an Incentive Project. The effective rate shall be subject to annual escalation equal to annual percentage increases in the Consumer Price Index (CPI) Housing Index for Boston-Brockton-Nashua, MA-NH-ME-CT or similar index to reflect changes in dollar values over time; however, annual decreases in CPI shall not cause the contribution rate to be decreased. The table below is intended to administratively track changes to the Housing Contribution Rate as it is adjusted over time."

Planning Board Action: Recommendation to City Council

Memo Contents: Information in response to questions raised at Planning Board and Ordinance Committee hearings

Update

The Planning Board held a hearing on this Petition on June 28, 2022, and the Ordinance Committee held a hearing on July 27, 2022. CDD staff provided a memo on the Petition dated June 22, 2022 (attached). Both bodies continued their discussions to a future date with no recommendation.

Various questions were asked at the hearings and this memo provides some information in response to those questions. Additional questions are addressed in a separate legal opinion from the City Solicitor.

Questions Raised at Previous Hearings

Questions related to how the current Petition could be amended prior to adoption, and related to what amendments to the Incentive Zoning requirements would be supportable by the most recent nexus study completed in 2019, will be addressed by the City Solicitor.

The following questions are related to planning issues.

Planning Board

- Clarify which uses are subject to Incentive Zoning and which are not.
- How do different land uses impact housing supply and demand?
- How does the Housing Contribution Rate affect small retailers?
- Is the cost of the Housing Contribution Rate passed on to tenants?
- Does the 30,000 square-foot GFA threshold adequately capture development projects that should be required to pay the Housing Contribution Rate?
- How does the proposed Housing Contribution Rate increase align with *Envision Cambridge*?
- Would the proposed Housing Contribution Rate slow development?
- What is the development community's response to the proposal?
- How much more money would be generated by the proposed Housing Contribution Rate increase? How many additional units of affordable housing would it create?

Ordinance Committee

- Provide the City Council a breakdown of the \$44 million dollars received since 2019 through the current Incentive Zoning program by project size.

Planning Board Questions

Which uses are subject to Incentive Zoning and which are exempt?

Incentive Zoning generally applies to non-residential development. Article 2.000 of the Zoning Ordinance specifically identifies the following uses listed in Section 4.30 of the Zoning Ordinance as being subject to Incentive Zoning if a project exceeds 30,000 square feet of Gross Floor Area (GFA):

- 4.31 i-2 (Hotel or motel),
- 4.32 f (Radio and television studio),
- 4.33 b-5 (College or University not exempt by statute, specifically including those uses and facilities listed in Subsection 4.56 c-4, c-5, and c-6),
- 4.33 c (Noncommercial Research Facility),
- 4.33 d (Health Care Facilities),
- 4.33 e (Social Service Facilities),
- 4.34 (Office and Laboratory Use),
- 4.35 (Retail or Consumer Service Establishments),
- 4.36 (Outdoor Retail or Consumer Service Establishments),
- 4.37 (Light Industry, Wholesale Business and Storage), and
- 4.38 (Heavy Industry).

All other uses listed in Section 4.30 are not subject to Incentive Zoning, including religious uses, other educational uses (including elementary schools and dormitories), and government facilities.

How do different land uses impact housing supply and demand?

The “nexus” for the Incentive Zoning requirement is based on the direct impact of a particular development on the City’s need to provide affordable housing. This does not account for the broader impact of economic development and job growth in Cambridge and across the region, which impacts affordability by increasing competition for housing overall, but is not linked to any one development or any one community.

The [2019 Nexus Study](#) that formed the basis for the current rates projected the number of employees by use and industry to calculate the number of workers demanding housing in Cambridge. The impact of each use on housing supply and demand varies based on a number of factors, including employment density (i.e., the number of employees per square foot), the average income for jobs in that industry, and the likelihood that employees will move to Cambridge. The Nexus Study determined that the percentage of new employees who are expected to demand housing in Cambridge is 26.5% for employees at educational institutions; 13.3% for office workers; 12.3% for retail, restaurant and hotel employees; and 11.3% for employees in research and development firms. The below table from the Nexus Study shows how these percentages interact with the projected number of gross new jobs per industry as well as the projected incomes of those employees:

Table 7. Distribution of Annual Earnings for Expected Jobs among New Employees Demanding Housing in Cambridge from New Development by Use and Earnings Level

Tenant Use/Industry	Gross New Jobs	Number Demanding Cambridge Housing	No. with Earnings below 50% AMI*	No. with Earnings below 50 to 80% AMI*	No. with Earning 80 to 100% AMI*	Total with Earnings Below 100% AMI*	No. With Earning at 100% AMI or Above*
Research and Development	5,000	565	15	77	15	107	458
Office—IT Related	5,539	737	59	89	39	187	549
Office-Other	2,155	287	84	98	38	220	65
Institutional	867	230	9	58	106	173	59
Retail and Personal Services	182	20	8	9	0	17	2
Restaurants	1,000	123	115	5	0	120	4
Hotel	120	15	5	9	0	14	1
Total	14,863	1,977	295	345	198	838	1138

*Income level for annual earnings from one employee; Totals may not agree due to rounding.

The demand for affordable housing was projected for these uses based on the total housing demand and the share of employees earning wages that qualify for affordable housing programs. For example, while IT-related office jobs will result in 737 new employees demanding housing in Cambridge, approximately 75% of those employees earn 100% or more of the Area Median Income (AMI). In contrast, while restaurants will result in 123 new employees demanding housing in Cambridge, only four of those employees earn 100% or more of AMI.

How could the proposed rate change affect the amount of funds collected? How many additional units of housing would it create?

The attached Policy Order Response summarizes Housing Contributions made in Fiscal Years 2019 through 2022. It shows that during those four years there has been approximately \$44 million in contributions made from about 2.7 million square feet of qualifying non-residential development. Because it typically takes 3-4 years for development subject to a particular rate to come to completion, most of these contributions are based on rates lower than the current \$21.02 per square foot.

The [2019 Nexus Study](#) projected approximately 5,840,000 square feet of new qualifying non-residential development over 10 years. This projection is highly variable due to market conditions and is a snapshot of the development climate at that point in time. The study recommended increasing the Housing Contribution Rate from \$17.10 to \$19.10 in the first year, then to \$23.10 (plus any adjustments for inflation) over four years. With a projection of roughly 600,000 square feet of qualifying development each year on average, that would result in roughly \$134 million (plus inflation) over 10 years, with roughly \$14 million (plus inflation) per year at the highest rate.

It is difficult to predict the effect of a higher rate on the pipeline of qualifying projects, as discussed further below. Assuming the same amount of annual development that was projected in the Nexus Study, the proposed rate of \$33.34 per square foot would result in about \$20 million per year in contributions, compared to \$14 million at the highest rate recommended by the Nexus Study. However, the actual amount of funding generated by the Housing Contribution Rate depends on the amount of actual qualifying development that is permitted. It also depends on any exemptions that are built into the rate system.

Incentive Zoning Housing Contributions are made to the Affordable Housing Trust, and are used by the Trust to create and preserve affordable housing. Incentive funds have been used to assist in the preservation of 166 affordable rental units as well as to create new affordable housing. The number of units created with Trust funds depends on many factors including the type of development, the specifics of the project, and what other fundings sources can be applied. For example, recent funding commitments for new affordable housing approved by the Trust have been in the range of \$150,000-\$200,000 per unit for rental housing. Commitments for new affordable homeownership units range up to approximately \$425,000 for units purchased through the HomeBridge program.

How could the rate change affect development? How could the rate change affect tenants, particularly retail tenants?

The [2019 Nexus Study](#) discussed the effect of the Housing Contribution Rate on developers and tenants (see pages 64-67). The main policy issue identified in setting the rate was how it would impact Cambridge's competitiveness in a regional real estate market. In other words, would a higher rate encourage developers to build in surrounding communities to get a better return on equity? Similarly, if higher contribution rates are passed along to tenants through higher commercial rents, could that encourage tenants to look for space elsewhere? The Nexus Study also discussed the impact that any additional commercial development, whether in Cambridge or in surrounding communities, would have on the regional housing market, which would in turn create more demand for housing in Cambridge.

The study evaluated these factors and noted that Cambridge's Class A office/lab market remained strong in relation to competing areas, even though Cambridge has a higher Housing Contribution Rate than communities such as Boston and Somerville. That showed a capacity to raise the Housing Contribution Rate, but the study cautioned against a sudden increase that would widen the gap between Cambridge and surrounding communities. The study recommended raising the rate gradually over time so that changes could be more easily absorbed into the market, thus lowering the risk of impacting Cambridge's competitiveness.

Recently, commercial laboratory development has expanded in inner core communities other than Cambridge, including Boston, Somerville, and Watertown. Those communities are currently in the process of reassessing their own housing linkage rates. These factors make it more difficult to assess impacts on competitiveness. Changes to the larger U.S. and global economy and recent increases in construction costs are also major factors affecting development that cannot be fully anticipated. The Nexus Study also noted concerns from developers about the uncertainty of how other City requirements might affect development costs.

Effects on retail uses are more complex. There is a nexus between retail uses and the need for affordable housing because retail and restaurant workers tend to have lower average wages than office and laboratory workers (see above). However, most new retail development in Cambridge is a smaller component of larger office/lab or mixed-use developments, where the goal is to promote activation and amenities for workers and residents. As a result, the cost of the retail space tends to be absorbed into the larger project, and in some cases is subsidized by the property owner. Different property owners might choose how much to subsidize retail rents to achieve their desired goals, but the Housing Contribution Rate is not likely to have a significant effect on that decision. Moreover, in some areas

where new ground-story retail is encouraged, it is exempt from GFA calculations, so it does not factor into the Incentive Zoning contribution. The scenarios where the effects might be more significant are on stand-alone retail developments of over 30,000 square feet, which are proposed from time to time but are relatively rare, as discussed below.

How appropriate is the 30,000 square-foot threshold?

The 30,000 square-foot threshold has been in place since the Incentive Zoning provisions were first adopted in 1988. Having a threshold is important because property owners need to have the ability to choose to undertake a project without being subject to the requirement. Subsequent nexus studies supported maintaining the 30,000 square-foot standard.

The following are some examples of projects that have been permitted in recent years that have been under the 30,000 square-foot threshold. Notably, many of them have been hotel developments. There are also a couple recent examples of smaller as-of-right office/lab developments, which had previously been less common.

Project Address	Uses	Non-Res. GFA	Status
38-40 Hampshire Street	Office/lab	15,834	Permitted 2021
38-40 Hampshire Street	Hotel	23,030	Permitted 2021, not built
55 Spinelli Place	Office/lab	17,094	Permitted 2021
263 Msgr. O’Brien Hwy.	Hotel	23,221	Permitted 2019
1991-2013 Mass. Ave.	Residential, retail, religious	21,632	Completed 2021
907 Main Street	Hotel, retail	29,860	Completed 2020
1924 Mass. Ave.	Hotel, retail	24,162	Completed 2016

For a variety of reasons, there tend to be few commercial developments between 25,000 and 50,000 square feet in size. Developers may try to avoid projects that are just over the 30,000 square-foot threshold, but the conditions of development sites and district zoning limitations tend to be stronger determinants of a project’s size. If the threshold were changed to a different number, a similar issue would arise at whatever new threshold is chosen. The suggestion of treating the threshold as a “deduction” – i.e., the first 30,000 square feet are not counted in calculating the Housing Contribution – could mitigate the impact on developments that are just above the threshold, but would reduce the total contribution amounts as it would apply to large and small developments. At the current rate of \$21.02, deducting 30,000 square feet would reduce contributions by \$630,000 per development.

What has been the reaction from the development community?

Thus far, comments have been received from the Chamber of Commerce, the Harvard Square Business Association, and property owners of medium-sized sites in areas such as Harvard Square and Central Square. The concerns have focused entirely on disproportionate impacts on smaller development sites and on retail or hotel development in particular, as discussed above.

No feedback has been received from larger-scale commercial property owners or developers, or from large institutional property owners or developers.

How does this proposal align with Envision Cambridge?

The [2019 Envision Cambridge comprehensive plan](#) establishes broad housing strategies to “Encourage affordable housing production for low-, moderate-, and middle-income households through regulatory and zoning incentives” and to “Expand resources for affordable housing production and preservation.” It sets a target of creating at least 3,175 new affordable housing units between 2017 and 2030, through a combination of inclusionary housing and directly subsidized affordable housing development. It also sets a target of increasing annual funding to affordable housing from \$13 million to \$20 million. It acknowledges Incentive Zoning as an important source of funding for affordable housing, along with Community Preservation Act and other public funding sources, but does not make specific recommendations as to the contribution rate.