



CITY OF CAMBRIDGE
COMMUNITY DEVELOPMENT DEPARTMENT

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MEMORANDUM

TO: Robert W. Healy, City Manager

FROM: Susan Schlesinger, ^{SS}Assistant City Manager for Community Development

DATE: June 18, 1997

RE: Recommendations on a New Inclusionary Zoning Ordinance

We are forwarding to you a copy of a report, "Recommendations Concerning a New Inclusionary Zoning Ordinance." This report provides recommendations to the City on establishing a policy to require the inclusion of affordable housing units in market-rate residential developments. The report has been prepared by Peter Werwath & Associates, under contract to the Community Development Department. A summary of the recommendations is found below.

City staff have worked over the past few months to analyze existing inclusionary zoning provisions, and to develop a new citywide policy that would increase the production of affordable housing in the City. Although the City has several districts with inclusionary zoning provisions, most have not succeeded in generating the production of any affordable housing units. We have taken the lessons from these existing provisions, and applied them in this report.

The recommendations include the following:

1. Any new ordinance should be mandatory, apply citywide and replace most of the existing inclusionary provisions of the City that now apply to residential uses in certain districts.
2. The ordinance should not alter the existing provisions linking new commercial and retail developments to affordable housing contributions (so-called linkage or incentive zoning provisions).
3. Mandatory provisions should apply to all new residential developments with 10 or more units. In addition, the ordinance should provide incentives for voluntary compliance by developers of smaller projects.

4. The resulting affordable units should be targeted to low- and moderate income residents -- with the average unit being affordable to a household with an income equal to 65% of the area median.
5. Using affordability formulas that are included in this report, the resulting affordable sale prices would average \$100,000 in 1997 dollars. Affordable rents would average \$777 per month plus utilities.
6. The required percentage of affordable units can be determined only after a rationale study (which is beyond the scope of this report) is completed. The rationale study is an economic analysis that provides the financial and legal justification for establishing an affordable housing requirement in market-rate residential developments. To model the effects of the proposed ordinance, we have presumed a 10 percent requirement, which is typical of many inclusionary ordinances.
7. Developers who comply with affordability provisions should be eligible for incentives in the form of additional allowable density, which should be granted by right. The additional allowable density should be approximately twice the percentage requirement for affordable units, e.g. a 20 percent bonus if 10 percent of the units are to be affordable. For smaller projects subject only to voluntary compliance, bonuses could be made possible (but not guaranteed) through a special permit process.
8. If the City deems an affected development as unsuitable for affordable housing, the City should allow the developer to build affordable units off-site or make an in-lieu payment.

We intend to commence immediately with the rationale study. This study will provide the basis for recommending the exact percentage of the affordable requirement in the policy.

We look forward to working together with you and the City Council to moving forward on drafting a new inclusionary zoning ordinance.

Attachment

**RECOMMENDATIONS CONCERNING A
NEW INCLUSIONARY ZONING ORDINANCE**

A REPORT TO THE CITY OF CAMBRIDGE

**By Peter Werwath and Associates
Damariscotta, Maine**

June 17, 1997

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EXECUTIVE SUMMARY

This report describes recommended approaches and options for the City of Cambridge to adopt broader inclusionary zoning provisions, with the intent of providing: (1) more affordable housing to low- and moderate-income Cambridge residents and (2) more economic integration of new housing built in the city.

The City's Community Development Department asked the authors of this report to make recommendations on the structure of a new inclusionary zoning ordinance that would be broader in scope and more effective than the inclusionary provisions presently in force in Cambridge. These are the key recommendations:

- Any new ordinance should be mandatory, apply citywide and replace most of the existing inclusionary provisions of the City that now apply to residential uses in certain districts.
- The ordinance should not alter the existing provisions linking new commercial and retail developments to affordable housing contributions.
- Mandatory provisions should apply to all new residential developments with 10 or more units. In addition, the ordinance should provide incentives for voluntary compliance by developers of smaller projects.
- The resulting affordable units should be targeted to low- and moderate income residents--with the average unit being affordable to a household with an income equal to 65% of the area median.
- Using affordability formulas that are included in this report, the resulting affordable sale prices would average \$100,000 in 1997 dollars. Affordable rents would average \$777 per month plus utilities.
- The required percentage of affordable units can be determined only after a rationale study (which is beyond the scope of this study) is completed. To model the effects of the proposed ordinance, we have presumed a 10 percent requirement, which is typical of many inclusionary ordinances.
- Developers who comply with affordability provisions should be eligible for a density bonus, which should be granted by right. The bonus should be approximately twice the percentage requirement for affordable units, e.g. a 20 percent bonus if 10 percent of the units are to be affordable. For smaller projects subject only to voluntary compliance, bonuses could be made possible (but not guaranteed) through a special permit process.
- If the City deems an affected development unsuitable for affordable housing, the City should allow the developer to build affordable units off-site or make an in-lieu payment.

METHODOLOGY

To form these recommendations, the consultants relied on their professional knowledge and experience, as well as review and analysis of the following documents and information:

- The City's zoning ordinance.
- The City's Consolidated Plan.
- Descriptions of inclusionary zoning programs that are active in other cities in Massachusetts and other states.
- A recent City report describing the pipeline of residential development projects in Cambridge.
- Internal City memoranda concerning existing inclusionary requirements and issues of concern in developing a new ordinance.

In two meetings, the consultants discussed the possible ramifications of a new inclusionary ordinance with City officials who are members of the Inclusionary Zoning Working Group: Susan Schlesinger, Assistant City Manager for Community Development; Roger Herzog, Housing Director; Les Barber, Director of Planning and Land Use; and Elizabeth Sternberg, Housing Project Planner.

Florrie Darwin, a member of the Planning Board and the Affordable Housing Trust, and Barbara Shaw from Just-A-Start Corporation also participated in the discussions. In addition, confidential interviews were conducted with two housing developers based in Cambridge who have produced, or have considered producing, affordable housing in conjunction with market-rate residential developments.

Peter Werwath performed the research and analysis and is the author of this report. Prior to the report being completed, Jerold Kayden, Esq. (as part of this study) advised both Mr. Werwath and City staff about the constitutionality and other legal ramifications of the proposed inclusionary provisions.

RECOMMENDED FRAMEWORK OF A NEW ORDINANCE

The following recommendations are made regarding the basic framework of the proposed inclusionary zoning ordinance.

- **There should be a combination of mandatory and voluntary provisions.**

For larger projects (with 10 or more units), mandatory provisions will be most effective in generating more affordable housing construction. For projects with fewer than 10 units, the ordinance should provide incentives for voluntary compliance.

- **For larger projects, density bonuses should be available as a matter of right, not subject to a special permit.**

To make the provisions efficient and effective for both the City and developers, the proposed density bonus incentive should be a matter of right when mandatory affordable housing provisions apply and are met.

- **A "rationale" study is needed.**

Prior to enacting any new inclusionary provisions, it is essential that the City conduct a rationale study that: (1) shows how market-rate housing development creates a need for affordable housing, (2) quantifies the need, and (3) ties that number to the inclusionary obligations.

Existing Inclusionary Provisions

In analyzing the effectiveness of inclusionary provisions, we were asked to limit our study to ordinances affecting residential construction. This leaves aside the City's affordable housing provisions in Article 11.200 of the zoning ordinances, since they apply only to non-residential construction. Henceforth, to simplify the discussion, requirements for non-residential development will be referred to as "linkage" provisions, while those affecting residential construction will be called "inclusionary" provisions.

Presently, inclusionary provisions are in force for five zoning districts: Residence C, Special District 9, Special District 10, the Cambridgeport Revitalization Development District and the North Point special district. The provisions--and their results--vary considerably from district to district, as follows.

Residence C - Compliance is voluntary and is subject to a special permit from the Board of Zoning Appeal. A density bonus of 25 percent is allowed if half of the resulting bonus units are made affordable (effectively requiring affordability in 10 percent of the total units). No affordable units have been built as a direct result of these provisions.

Special Districts 9 and 10 - Compliance is voluntary and is subject to a special permit. The allowed number of units can be increased by 125 percent, while the minimum floor area ratio (FAR) is increased from 63 percent to 108 percent, depending upon the number of affordable units built. Limitations on building heights and setbacks can be relaxed. Of the total number of units

built, at least 16.5 percent must be affordable. No affordable units have been built as a direct result of these provisions.

Cambridgeport Revitalization Development District - Compliance is essentially mandatory if property owners wish to build non-residential structures. To achieve a full non-residential build-out, a total of 400 residential units must be built, of which 150 must be affordable. A total of 100 units must be occupied by households with incomes at or below 80 percent of the area median income, and 50 by households with incomes at or below 110 percent of median income. Of the 150 required affordable units, 114 have been built in two projects: Kennedy Biscuit Lofts and Auburn Court.

North Point Residence, Office and Business District - Compliance is voluntary and subject to a special permit. The allowed FARs can be increased as much as 250 percent, and building height limitations can be waived entirely, but a minimum of 7.5 percent of the dwelling units must be affordable. To date, a total of 33 affordable units are under construction in the Museum Towers development.

The Need for a New Ordinance

In analyzing these existing inclusionary provisions, it is clear that they have been effective in only two circumstances: (1) where they are quasi-mandatory (Cambridgeport) and (2) where the density bonus is exceptionally generous (North Point). After discussing these results with City staff and several developers, the following conclusions were drawn about the weaknesses of the current provisions:

- Most voluntary provisions with density bonuses are not working.
- The need for special permits discourages participation, since it leads to an unpredictable and time-consuming public approval process.
- In other respects, the ordinance provisions (particularly for districts C, 9 and 10) are too complex and leave too many requirements subject to negotiation.
- Limitation to certain districts reduces the potential output of affordable housing.
- All of the resulting affordable housing has been built in projects ranging in size from 77 units to 435 units--suggesting that existing incentives have not been attractive or feasible for developers of smaller projects.

Thus, we propose new provisions that: (1) are mandatory, (2) do not require special permits (in most cases), (3) apply citywide, (4) are simpler and (5) allow for special treatment of smaller developments. The details are spelled out in the remainder of this report.

APPLICABILITY

The following recommendations are made regarding the applicability of the proposed inclusionary zoning ordinance.

- **In general, mandatory inclusionary provisions should apply to any residential development with 10 or more new or substantially rehabilitated dwelling units.**

Special residential uses such as dormitories and group homes would not be affected.

- **In general, the provisions should apply citywide.**

The provisions should generally apply to all zones in which residential development could be approved by the City, including non-residential zones in which a change of use might occur. However, the recommended 10-unit threshold will likely make the provisions more effective outside of existing, low-density residential neighborhoods, where most developments tend to have fewer than 10 units.

- **The ordinance should clearly spell out its effective date.**

We recommend that the ordinance be made effective as of the date of enactment by the City Council. The ordinance should grandfather any residential developments for which an application has already been made, as of the effective date of the ordinance, for any form of City development approval.

Existing Linkage Provisions Should Be Unaffected

The study did not address the creation of any new linkage requirements. The City already requires commercial developers to support affordable housing through linkage provisions. One could argue that inclusionary requirements for both commercial and residential developments could be combined in one ordinance. However, that approach would not be practical. The basis for--and the mechanics of--the proposed requirements for residential developments would differ substantially from the linkage requirements already in place.

Basis of "Threshold" Recommendations

The recommended threshold of 10 newly-created dwelling units for mandatory compliance is based on three factors: (1) the desirability of removing the burdens of compliance on developers of smaller projects, (2) precedents in other communities with inclusionary zoning ordinances and (3) the fact that the density bonuses proposed herein have diminishing benefits for projects with fewer than 10 units.

The proposed threshold has two precedents in Massachusetts. Brookline's and Newton's mandatory inclusionary ordinances set the same threshold of 10 dwelling units (either new construction or reuse). In contrast, Cambridge's existing inclusionary provisions require no thresholds because compliance is only voluntary.

Still, a considerable amount of residential development in Cambridge occurs in small-scale

projects that are appropriate for inclusion of affordable housing. As an inducement to this occurring in at least some cases, we propose that density bonuses be made available to developers of projects with fewer than 10 units who voluntarily agree to comply with the ordinance. (However, as we will explain later, this may not be an effective incentive for very small projects.)

What about existing dwelling units in an affected development that are untouched or undergoing only moderate rehabilitation? We propose that these dwelling units not be counted toward the threshold—only units that are new or substantially rehabilitated. Naturally, this provision will require that the ordinance define substantial rehabilitation.

Citywide Impact

The main impetus for the City's investigation of new inclusionary provisions is the desire to generate more construction of affordable housing. One effective way to accomplish this is to make the provisions apply throughout the city (with the exception of certain districts noted below). Although citywide provisions may have little or no impact in some zoning districts and neighborhoods, that is no reason to exempt the occasional projects in those areas that would be subject to mandatory inclusionary provisions.

Exceptions for Two Special Districts

Nonetheless, special provisions should still apply to the Cambridgeport and North Point special districts. Existing inclusionary provisions for the Cambridgeport special district should be left untouched, while provisions for the North Point district might be modified somewhat.

The Cambridgeport district is a unique situation where inclusionary provisions have worked and the affordable housing requirements are well on their way to being fulfilled. In the North Point district, generous density bonuses (more generous than we propose citywide) have worked, and there is no obvious reason to remove them. However, in other respects, provisions for the North Point district should conform to the new, standardized citywide requirements.

Grandfather Clause

It is recommended that the City grandfather any proposed developments which have formally applied for any type of development approval from the City prior to the effective date of the ordinance. However, this should not prevent a developer from voluntarily re-submitting a proposal to comply with the new ordinance and receive a density bonus.

AFFORDABILITY REQUIREMENTS

The following recommendations are made regarding the requirements for the affordable units built in compliance with the ordinance.

- **The beneficiaries of affordable units**

All beneficiaries should be households with incomes at or below 100 percent of the area median income (the prevailing standard for low- and moderate-income households). Further, the average beneficiary should be a household with an income at 65 percent of the area median income.

- **Types of tenure (i.e. rental and ownership)**

The tenure of affordable units should mirror the project as a whole. For example, affordable units should be sold, not rented, where a majority of units will be offered for sale.

- **Required number of bedrooms and bathrooms**

Typically, affordable rental units should have two bedrooms and one bath, while affordable for-sale units should have three bedrooms and one and a half bathrooms ("prototype sizes"). In a project with two or more affordable units, staff should have the discretion to negotiate for a reasonable mix of bedroom/bathroom sizes, the average of which approximates the prototype sizes.

- **Pricing formulas**

Pricing formulas in Appendix A were used to establish prototype rents and sale prices affordable to a household with an income equal to 65 percent of the area median. In projects with two or more affordable units, staff should have the discretion to negotiate a mix of higher and lower rents or sale prices, the average of which approximates the prototype prices.

This income standard translates to these currently affordable prices:

3-bedroom for-sale unit	\$100,000
2-bedroom rental unit (without utilities)	\$777/mo.

- **Residency preference for buyers/renters**

Affordable units should be marketed with a preference for households that have resided in Cambridge for at least a year.

Existing Income Standards Used by the City

Regarding the incomes of beneficiaries, our recommendations vary somewhat from the City's existing inclusionary provisions for residential developments. For example, the existing

provisions for Special Districts 9 and 10 target households with incomes ranging from "very low" (below 50 percent of median income) to "low" (50 to 80 percent of median income), to "moderate" (80 to 100 percent of median income). In order for developers to receive density bonuses, they must deliver units in each price category--first, the lowest-priced unit, then two middle priced units, then the highest-priced unit, and then rotating back through that order.

Prototype Unit Sizes and Prices

We believe it is simpler, more flexible and more predictable for the City to establish prototype sizes (by number of bedrooms) and prototype prices in only two categories--rental and for-sale housing. This allows developers to make more reliable financial projections. Staff should have the discretion to negotiate with developers to skew prices and bedroom sizes of the affordable units over and under the prototype numbers.

Without this skewing, affordable units would serve too narrow a range of household incomes and family sizes. However, to cast in stone a formulaic mix of prices and unit types is not deemed advisable. Reportedly, developers have found it difficult to comply with the formulas of the existing ordinance, in part, because of their complexity. Besides, some projects will lend themselves better than others to offering a broader range of prices and unit types.

Basis of Proposed Income Standards

We believe that a 65 percent standard follows the intent of the existing ordinances. Moreover, it is a reasonable compromise between: (1) the income profile of Cambridge residents who most need affordable housing and (2) the financial impact of this standard on developers.

It goes without saying that the lower the income standard, the lower the required rents and sale prices must be and the larger the financial impact on developers. On the other hand, the City's own Consolidated Plan asserts that renter households with incomes below 50 percent of median income face the highest housing cost burdens--with 65 percent of this group paying more than 30 percent of their incomes for rent.

Preference for City Residents

In keeping with current policies of the City regarding assisted housing, we recommend giving Cambridge residents a preference for buying or renting the affordable units.

QUALITY STANDARDS

The following recommendations are made regarding the quality of the affordable dwelling units to be provided.

- **Minimum square footage**

To ensure livability, affordable units should have the following minimum square footages of living space:

	For-Sale Units	Rental Units
1-Bedroom	750	650
2-Bedroom	950	800
3-Bedroom	1,100	950
4-Bedroom	1,250	1,000

- **Finishes and amenities**

The City should impose minimum standards to assure durability, energy efficiency and water conservation. In addition, exteriors of affordable units should closely resemble the exteriors of other units in a project, and residents of affordable units should have the full use of all amenities in the common spaces.

Problems with Existing Requirements

Our recommendations are somewhat less stringent than the existing inclusionary requirements. For example, the rules for Special District 9 and 10 are as follows:

Existing requirements:

One-bedroom units are not allowed	
Minimum size of two-bedroom units:	1,100 square feet
Minimum size of three-bedroom units:	1,250 square feet
Minimum size of four bedroom units:	1,350 square feet

We believe there are three problems with the existing floor area requirements. First of all, they do not reflect the fact that rental units tend to be smaller than for-sale units. Second, it is possible to design livable units that are smaller. Third, the cost of any unnecessary square footage adds extra cost burdens for developers, who will face a substantial cost impact in any case.

Recommended Space and Quality Standards

We have suggested a standard for minimum square footages that closely tracks the requirements of the federal Rural Housing Service. To the best of our knowledge, these are the only remaining federal standards that address the issue of minimum, livable floor space. Tens of thousands of decent dwellings have been built to those standards.

Our recommendations on finishes and amenities closely track the City's existing inclusionary provisions.

OTHER DESIRABLE AFFORDABLE HOUSING PROVISIONS

In order to make a new inclusionary zoning ordinance as effective and efficient as possible, these other provisions are recommended.

- **Substitution of off-site housing or in-lieu payments**

For projects subject to inclusionary provisions, the ordinance should allow developers to build units off-site or make an in-lieu cash or in-kind contribution if the City determines that the site or the proposed project is unsuitable for applying some or all of the provisions of the ordinance.

- **Nature and duration of long-term affordability controls**

Affordable rent levels should be maintained for 50 years in accordance with current practices of the City. Likewise, with for-sale units, the City should replicate its current system of deed restrictions controlling resale prices.

- **Non-permitted uses of capital subsidies**

Developers should not be permitted to use subsidized capital financing, to the extent that this allows them to externalize the costs of compliance with the proposed ordinance.

- **Treatment of projects with a substantial number of subsidized, affordable units**

Projects with a substantial percentage of affordable units subsidized through local, state, federal or philanthropic sources should be considered as automatically complying with the affordability requirements. The exact percentage should be determined after a rationale study is concluded.

Alternative Means of Compliance

In most cases, affordable housing requirements should be met by construction of affordable units on-site, rather than providing units off-site or making a financial contribution. This approach has two benefits: (1) it will ensure more economic integration of low- and moderate-income families, and (2) it will spare the City of the difficulties of converting cash to affordable units.

Nonetheless, strict adherence to this principal could have adverse results in some cases. For example, in some luxury condominium projects, low-income buyers could spend most of their housing budget on condominium fees, reducing or eliminating their ability to pay any debt service. In addition, some sites might be distant from public transportation, shopping areas and services, making them less suitable for low-income families.

Thus, we recommend that the City develop criteria by which the City would determine if and when alternative means of compliance are appropriate. City staff (not a developer) should determine when these criteria apply and whether an in-lieu payment or off-site housing should be substituted.

Determining the In-Lieu Payment Amount

The essential purpose of the in-lieu payment is to provide the City with funds to build—or cause to be built—affordable housing that is of equal value to the affordable units that otherwise would have been built on site.

Thus, the formulation of an in-lieu payment amount should be based upon three numbers:

1. The added land value that accrues to the project as a result of the density bonus.
2. The average cost to subsidize an affordable housing unit in Cambridge, apart from "inclusionary" units.
3. The amount of internal subsidy that would have been required to produce an affordable unit in the subject project.

The first number should be the "ceiling." In other words, the City should take back from the developer no more value than the density bonus has created.

The second number should be the "floor"—the payment should be no lower than this. Currently, City staff calculates the average capital subsidy for an affordable housing unit in Cambridge at approximately \$80,000. The ordinance should require staff to annual revise this floor amount based on current costs.

This third number—what the internal subsidy would have been—could guide the City in fixing an in-lieu payment amount where the developer disputes the City's estimate of land value added by the density bonus. For the City to calculate this amount, the developer would be required to disclose (in confidence) detailed financial projections for the project.

Long-Term Affordability

Regarding long-term affordability of the housing provided, the City appears to have well-established systems for both rental and for-sale housing. These should be referenced in any proposed ordinance.

Use of Capital Subsidies

The use of capital subsidies to produce the required affordable units is a thorny issue, and one that is not often addressed in the inclusionary zoning programs of other cities. The issue, in a nutshell, is whether the costs of providing affordable units should always be internalized within a project, or whether they can be externalized through the use of subsidies (keeping in mind that taxpayers provide the vast majority of housing subsidies).

In short, there is little point to having an inclusionary zoning ordinance if this use of subsidies is not prohibited. The ordinance will likely produce 30 or 40 affordable units a year, at best. The housing subsidies available in Cambridge each year are finite, and have shrunk drastically over the years.

So, unless developers are prohibited from using subsidies to externalize their costs, a likely scenario is that the available subsidies will simply gravitate toward "inclusionary" projects and thus result in a decrease in "non-inclusionary" affordable housing projects. This would negate the public benefits of the ordinance.

There should be one caveat to this prohibition of external subsidies. Nothing should prevent a developer from using outside subsidies to make rents or sale prices lower than required by the new ordinance or to provide more than the required number of units.

Compliance Standards for Subsidized Housing Projects

Beyond that, the City should not discourage the use of housing subsidies in any residential development. Therefore, we propose that projects with a substantial amount of subsidized, affordable housing—with, for example, two times the percentage required in the ordinance—be considered as complying automatically with the affordability requirements of the ordinance. Thus, such projects would qualify for the proposed density bonus without having to meet the exacting affordability requirements of the ordinance. This will simplify the plan submission, review and approval processes.

If provisions such as these are approved, subsidized housing could be built and considered in compliance with the ordinance even if the rents or sale prices were somewhat higher than those required by the ordinance, or if the square footage or other construction requirements were not quite met. But as a trade-off, such developments would provide a more ample amount of below-market-rate housing.

DEVELOPER INCENTIVES

The following recommendations are made regarding proposed incentives for developers.

- **The ordinance should provide for a percentage density bonus that is twice the percentage of required affordable housing.**

For example, if the developers of a 10-unit project were required to build one affordable unit (a 10% requirement), the allowed number of dwelling units and the maximum floor area ratio (FAR) should be increased by 20 percent, allowing 12 units to be built without reducing the average square footage per unit.

- **Design review by staff only to expedite approvals**

Even though density bonuses have been proposed as automatic--without the more stringent review process that comes with a special permit process--projects with density bonuses should be subject to design review by the City. However, as an additional incentive to developers, design review of inclusionary projects should occur only at the staff level, thus expediting the approval process, unless a special permit or variance were required for other reasons.

The Need for Density Bonuses

Without a doubt, any new inclusionary affordable housing ordinance will be ineffective without a density bonus. Virtually every inclusionary program in the United States contains a density bonus and in some cases other incentives to offset the cost of providing affordable housing.

The economic impact of inclusionary provisions is a complex issue. But, simply put, the purpose of most such provisions is to produce housing units at below-market prices. If the affordable housing units produced are of good quality, in most cases this requires developers to offer the affordable units at a discount to their market value. Obviously, this discount will reduce, or could even eliminate, profits unless there is some offsetting benefit to developers. Thus, density bonuses and sometimes other incentives are provided to offset those negative financial impacts.

In the narrative above, we noted that the average capital subsidy cost of an affordable housing unit in Cambridge is presently \$80,000. "Subsidy cost" and "discount to market value" are very similar concepts. Both are measures of the gap between what housing costs to develop and what low-income people can afford. Thus, one can reasonably assume that developers' negative financial impact of producing one affordable unit is at least \$80,000. (We say, "at least," because most affordable housing in Cambridge is built on the lower-cost residential land.)

However, this negative impact can be canceled out by the positive economic impact of a density bonus. In simplistic terms, a bonus allows a developer to build x-percentage of additional dwelling units. In real estate markets such as Cambridge with high market demand, each additional bonus unit creates an additional value in the land--which to a developer is almost equivalent to "found money."

Economic Impact of Proposed Density Bonus

On typical sites in Cambridge, we estimate that this added value of a bonus unit will be something on the order of \$40,000 to \$80,000 (depending upon the site location) and will average about \$50,000.

Based on this estimate, it seems appropriate to provide--where affordable housing is mandatory--two "bonus units" for each required unit of affordable housing. The value of two bonus units should create a "credit" of at least \$80,000. In comparison, the "debit" for producing one affordable unit will also equal a minimum of \$80,000.

If the cost of producing an affordable unit exceeds \$80,000 in some projects (as it undoubtedly will), this will be mostly due to the projects being built on higher-cost land. However, the added value of the density bonus will increase as land value increases. Thus, the bonus formula we propose should, in most cases, offset the cost of providing the affordable unit.

To summarize:

Minimum "debit" from providing affordable unit	\$80,000
Minimum "credit" from receiving two bonus units	\$80,000
Net financial impact in this scenario	\$0

Mitigations Needed for Smaller Projects

Unfortunately, this equation will not hold true with projects that are substantially smaller than 10 units. For example, envision a developer of a five-unit project that wants to build one affordable unit. Under the scenario just described, the project would qualify for only one bonus unit, since 20 percent of five is one. In this case, we would assume that the "credit" from the density bonus would probably be far less than the "debit" of providing one affordable unit.

Nonetheless, we stand by our proposal that density bonuses be capped at approximately twice the required percentage of affordable housing, for two reasons. First, higher density bonuses would amount to an unnecessarily generous incentive for most projects. Second, since the provisions are proposed to be citywide, making substantially higher density bonuses available to smaller projects would in some cases be certain to create adverse effects, particularly in traditionally residential neighborhoods.

But the City could find other ways to mitigate these potential problems with small projects. One way is to make its standards for rental rates or sale prices less stringent in these cases. For example, if only one bonus unit could be provided for an affordable unit (instead of two), the City could raise its standard for an affordable sale price from \$100,000 to \$140,000--lessening the developer's "debit" for providing affordable housing. The social benefits would be less, but still of value.

Relationship of Bonuses to Required Minimum Lot Areas

As a practical matter, the City would not actually allow "bonus units"--instead, it would reduce what the City ordinances call the "minimum lot area per dwelling unit." For example, if a 20 percent bonus were intended, the City would reduce this minimum lot area by 16.68 percent. This is illustrated by the following example:

C-1 District requirements (example):

Typical lot size:	12,000 square feet
Current minimum lot area per dwelling unit:	1,200 square feet
Current maximum number of dwelling units:	10
Reduce minimum lot area by 16.68 percent, to:	1,000 square feet
Resulting maximum number of dwelling units:	12

Issues with FARs

The allowed number of dwelling units on a site are limited by the City ordinances in two major ways: (1) the minimum lot area per dwelling unit (as just described) and (2) the maximum floor area ratios (FARs), which limit the maximum floor area that can be built per square foot of land. Naturally, both the minimum lot area and FAR vary considerably from one zoning district to another.

In some districts in Cambridge, the FAR can be a much more limiting factor than the minimum lot size. Therefore, to be effective, any new ordinance should also provide a bonus on the FAR ratio. We recommend that the size of this bonus be equivalent to the "unit bonus." For example, if the unit bonus is 20 percent, the FAR ratio should be 20 percent higher than the base FAR in order to allow construction of units of the same size.

ADMINISTRATIVE IMPLICATIONS

Proposed Administration by Community Development Department

Because the City presently administers inclusionary provisions in special districts, the administrative implications of the proposed new ordinance are well known and need little discussion.

The City's Community Development Department presently takes the responsibility for negotiating, monitoring and enforcing the existing provisions. The role of the Building Inspection Department is simply to ensure that development proposals have met the requirements before permits are issued. These roles seem appropriate and should be the model for any new ordinance.

Expected Annual Output from Proposed Ordinance

To determine both the benefits of the proposed new ordinance and its administrative implications, it is necessary to make a projection of annual market-rate residential construction starts to which the mandatory provisions would apply. To do so, we reviewed Cambridge's development pipeline, leaving out projects with fewer than 10 units and without substantial numbers of subsidized housing units.

We found that only three projects meeting these criteria started construction last year. The projects contained a total of 678 units. If the proposed ordinance had been in effect during that year, with a 10 percent affordability requirement, 67 affordable units would have been obligated. As it was, 33 affordable units were actually obligated in the North Point district.

This volume of residential construction is much larger than the levels experienced in any other recent year, and it is impossible to predict if this pace will be sustained. Thus, a conservative estimate of the annual output of a new inclusionary ordinance would be more on the order of 30 to 40 affordable units. Obviously, this number will be affected by the percentage of affordable units that is selected by the City based on a rationale study.

Implications of By-Right Bonuses

The recommendation of "by-right" density bonuses, except in the case of projects with fewer than ten units, has major administrative and political implications for the City.

In the preceding section on developer incentives, we have already stated our case for by-right bonuses. In sum, we feel automatic bonuses would be a very positive incentive for developers to participate in providing affordable housing, whether that is done on a mandatory or voluntary basis. It will hasten their approval time and, thus, reduce the costs of development. It also removes uncertainties regarding special conditions that might be imposed on the development and further increase costs.

Such a system would give City staff--presumably with the Community Development Department in the lead--the complete responsibility for performing design review and site plan review.

However, as desirable as this approach is from the standpoint of efficiency, it is likely to generate opposition from some citizens and perhaps elected officials who are concerned about higher-density development and want a voice in the approval process. That participation would occur only if the bonuses were granted through special permits.

The City, then, must make a hard choice between: (1) by-right bonuses and the benefits of expedited approvals and (2) requiring special permits and, thus, providing for citizen and Planning Board participation in granting the proposed bonuses. We strongly recommend the first option.

NEXT STEPS

If the findings and recommendations of this report are generally acceptable to the City, we suggest the following as next steps.

- The City should conduct a study that quantifies the economic relationship between new residential development in Cambridge and the need for additional affordable housing units.
- The study should specifically describe need for affordable housing—expressed as a fractional number of affordable housing units—generated by construction of new market-rate units. The number will likely fall in the range of .10 to .20 (based on our experience in other communities).
- Then, an ordinance can be developed with a percentage requirement of affordable housing which should not exceed that number, but could be lower.
- Only after the percentage requirement for affordable housing is determined should the City arrive at a percentage density bonus—along the lines laid out in this report.
- Based on an assessment of political and administrative considerations, the City should decide whether the proposed density bonus should be granted by right or through a special permit process.
- With these key variables determined and approval (in concept) by the City Council, City staff should then proceed to draft an ordinance for the Council's review and approval.

APPENDIX A: AFFORDABILITY CALCULATIONS

PROTOTYPE 3-BEDROOM FOR-SALE UNIT

Following are steps in calculating the sale price of a three-bedroom home that is affordable to a prototype household with an income equal to 65 percent of the area median.

Presumed average household size for 3-bedroom home: 4 persons

Area median income for 4 persons (from HUD): \$59,600

Income level to be served: 65% of area median

Multiply 65% (.65) times \$59,600. The result is: \$38,750

Determine income per month (\$38,750 divided by 12): \$3,228

Presumed percentage of income affordable for a mortgage payment, including principal, interest, taxes and insurance: 28%

Presumed percentage of income affordable for principal and interest only, with 6% allowed for taxes, insurance and condominium fees: 22%

Multiply 22% (.22) times \$3,228 to determine affordable monthly loan payment: \$710

Determine affordable rate and term of loan: 8.25%, 30 years

Determine affordable loan amount (from tables or calculator): \$94,712

Affordable loan amount (\$94,712) divided by 0.95 (assumes a 5 percent down payment) and round to nearest thousand. Equals affordable purchase price: \$100,000

PROTOTYPE 2-BEDROOM RENTAL UNIT

Following are steps in calculating the monthly rent of a two-bedroom unit that is affordable to a prototype household with an income equal to 65 percent of the area median.

Presumed average household size for two-bedroom rental unit: 3 persons

Area median income for 3 persons (from HUD): \$53,600

Target income level: 65% of area median

Multiply 65% (.65) times \$53,600. The result is: \$34,850

Determine income per month (\$34,850 divided by 12): \$2,904

Presumed percentage of income affordable for rent and utilities: 30%

Multiply 30% (.30) times \$2,904 to determine affordable monthly payment: \$871

Determine an average-case utility allowance for a 2-bedroom unit: \$94

Subtract \$94 from \$871. Result equals affordable rent: \$777