

**OFFICE OF INDEPENDENT BUDGET ANALYST
CITY OF SAN DIEGO
M E M O R A N D U M**

No. 06-2

DATE: March 17, 2006

TO: Council President and City Council Members

FROM: Andrea Tevlin, Independent Budget Analyst

SUBJECT: Inclusionary Housing – Timing of In-Lieu Fee Calculations

On Tuesday, March 21 the Ordinance amending the City's 2003 Inclusionary Housing Ordinance regarding the timing of the fee calculation is scheduled for the City Council (Item #333). Currently, the in-lieu fee is calculated at the time the building permit is issued. The Building Industry Association (BIA) is requesting to change the calculation of the in-lieu fee to the time the first application for development is deemed complete. In 2003, the BIA filed a lawsuit against the City of San Diego regarding the interpretation of when the in-lieu fee should be assessed.

The City Council requested an analysis by the Independent Budget Analyst to analyze any fiscal impact to the City regarding the timing of the in-lieu fee calculations.

A developer can choose to pay an in-lieu fee as an alternative to constructing the affordable housing units according to the Ordinance. The current fee is \$2.50 per sq. ft. The following shows the history of the in-lieu fee:

- July 3, 2003 \$1.00 per sq. ft.
- July 3, 2004 \$1.75 per sq. ft.
- July 3, 2005 \$2.50 per sq. ft.
- July 3, 2006 estimated \$7 – 10 per sq. ft. *(still under review)*
- July 3, 2007 *TBD based on the real estate market (including the median priced home and the area median income)*

The time the first application for development is deemed complete to the time an application for a building permit is filed can be any where from 6 to 18 months. This time is a review process that includes several reviews by City staff, Hearing Officer, Planning Commission, and the City Council. If a developer decides to build the affordable units as opposed to paying the in-lieu fee, the process is expedited to approximately 6 to 9 months.

The process to obtain a permit depends on the scope of the project and various regulations. The City of San Diego is currently in the process of evaluating the City organization, and may want to evaluate through the Business Process Reengineering the length of time it takes developers to receive a building permit from the time the first application for development is deemed complete.

The San Diego Housing Commission report states the following:

“...the gap represented by when the in-lieu fee is assessed and when the fees are paid could have significant impacts on the collected in-lieu fees’ impact in future years. Such results are unquantifiable at present due to the fact that the in-lieu fee shall progress to a formula on July 3, 2006 which will take into consideration figures that will be ascertained each year.”

In an attempt to quantify the impact to the City of San Diego and the developers, a hypothetical example will be used. If a developer with a building of 100,000 sq. ft. submitted an application on November 2004 (\$1.75/sq. ft.), the in-lieu fee based on the BIA’s requested calculation at the first deemed completed application, would have totaled approximately \$175,000. If the building permit was not issued until August 2005 (\$2.50/sq. ft.), the in-lieu fee based on the current calculation at time of building permit, would total \$250,000. That is a difference of \$75,000. If the building permit is issued on August 2006 (approx. \$7/sq. ft.), then the in-lieu fee may total \$700,000. There could also be extensions granted to developers up to nine years. Each year, the in-lieu fee could adjust depending upon the real estate market including the median priced home and the area median income (AMI).

This is a definite fiscal impact to the City of San Diego and the developers. One of the goals of the City should be to improve the length of time; whereby, the first application for development is deemed complete to the time an application for a building permit is filed. But clearly, if the City of San Diego amends the Ordinance to change the calculation of the in-lieu fee from the time an application for a building permit is filed to the time the first application for development is deemed complete, the fiscal impact to the City could be substantial depending upon the number and types of projects and other factors.

Based on the City Attorney’s Office’s legal analysis, the only other legal option would be to re-assess the fee each time the developer extends the project’s development approvals. This option would allow for the fee to be re-assessed every three years in the event that extensions are granted to developers. This option may still have a fiscal impact to the City depending upon the projects. The San Diego Housing Commission report states that if the City Council were to change the current procedure, the Housing Commission Board and the BIA have come to an “understanding” that both parties would agree to this option. However, the San Diego Housing Commission and City staff recommend the current procedure of calculating the in-lieu fee from the time an application for a building permit is filed.

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cc: Honorable Mayor Jerry Sanders