Homeownership Outcomes

While homeownership is generally valued by individuals, neighborhoods, and policymakers, affordable homeownership outcomes under the Ordinance have been mixed. Although 74% of market units were developed as homeownership units at the time of the 2007 assessment, only about one-fourth of the affordable units were homeownership. Currently slanted toward deep affordability and long affordability via strict requirements on equity gain, the homeownership option often presents significant challenges for developers, buyers and administering agencies. Outcomes and challenges are explored below as well as the inherent conflict between affordability and individual wealth building typically associated with homeownership.

Goals of Affordable Homeownership

How affordable homeownership programs align with seemingly conflicting goals influences program outcomes as well as key design features such as resale controls and equity share.

> <u>Creation of long-term affordable housing units.</u> When the difference between market and affordable prices is large, ordinances may be structured, for policy and legal reasons, to prevent windfall profits to the initial buyer and to ensure that more than one household benefits. Jurisdictions with this goal typically have strict re-sale provisions, requiring that, during the regulatory period (typically 30 years), the home be re-sold at an affordable price to a new income-eligible buyer. Because incomes rise at a slower and steadier pace (approximately 2% per year) than market prices, especially in a rising market, the affordable seller is very limited in the equity they can realize in their home. This is the current model of the City's inclusionary ordinance.
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> <u>Wealth building for lower income families.</u> This goal aims to promote homeownership as a means to increase stability and income. This goal is reflected in programs serving buyers just out of reach of the market and where the homeowner benefits from a greater share of the equity. In some cases, the buyer can sell the unit at market price and the buyer benefits from a greater share of the equity. After sale, the unit ceases to be affordable, and the jurisdiction may use their share of the equity towards other affordable housing goals. In other cases, the unit is still affordable on sale, but the jurisdiction contributes funding to allow a greater equity share. Three potential models include:
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> 1. Providing homeowner equity based on years of occupancy, e.g. 1/30th of the market appreciation per year owned.
> 2. Providing homeowner equity based on the initial proportional share of the developer subsidy to the market value of the home.
> 3. Providing homeowner equity on a "graduated" basis, with limited homeowner appreciation up front to discourage flipping homes and then allowing much greater homeowner appreciation for the remainder of the regulatory term.

Graphs showing the equity share models discussed above, including the current model will be shared at the meeting.

Note: Affordable homeownership is most typically achieved in government programs by offering favorable financing to assist buyers purchase homes. As an example, the California Housing Finance Agency provides first mortgage financing with interest rates generally below market. Additional financing tools include subordinate deferred payment or "soft" second mortgages that can provide mortgage interest buydowns, downpayment assistance, and closing cost assistance. These programs do not face quite the same challenge as regulated affordability because the assistance is structured as a loan that is repaid or a small grant.

Homeownership Outcomes

Inclusionary Homeownership to Date

In the 2007 assessment, staff shared these facts on homeownership under the ordinance:

- 23% of the constructed and approved units were ownership;
- Most of the inclusionary homeownership units were in small, single family subdivisions who could not partner with an affordable rental developer;
- In large Planned Unit Developments (PUDs), on average, 74% of the market units were ownership, but only 3% of the inclusionary units were ownership; and
- The average income of inclusionary homebuyers was 68% of area median income.

Staff has also looked at data on the 150 closed loans and found the following:
- 23% were very low income units and 77% were low income units
- 54 buyers (36%) received mortgage assistance from SHRA, and the average assistance amount was $24,000
- Three inclusionary units (2%) have gone into foreclosure
- 17 inclusionary units have been offered for resale, with five sold and 12 remaining unsold

Challenges of Inclusionary Homeownership Outcomes

Ordinance homeownership provisions create challenges to developers, buyers and SHRA and have unintended outcomes.

✓ <u>Income Targets</u>: The ordinance requires that homes be sold between 50% and 80% of area median income.

✓ <u>Sales Price Calculation</u>. Families are eligible at a range of incomes (very low incomes range from 31% to 50% AMI and low income range from 51% to 80% AMI); however, maximum prices are set at the top of the range.

✓ <u>Restricted Equity Share.</u> The ordinance has very limited equity share provisions; the inclusionary homebuyer receives only the increase in affordable sales price (based on the increase in AMI from the previous year).

✓ <u>Restricted Sales.</u> Sales are restricted to the same income categories as the original sale.

<u>Developer Challenges and Outcomes</u>

✓ <u>Option not chosen.</u> In the height of the market, affordable prices were about <u>*half*</u> of the median market sales price and so, when given a choice, developers did not choose the affordable homeownership option.

✓ <u>Product is less.</u> While the ordinance allows for some variation in amenities and size between inclusionary units and their market counterparts, some of the products built have been dramatically different. When this occurs, the units are not attractive or marketable, and the builder has had difficulty in selling the units.

✓ <u>Challenging to market.</u> Although the range of eligibility is adequate, because prices are set at the highest income of the range, many prospective buyers cannot qualify for a loan. This presents a serious marketing challenge to developers.

Homeownership Outcomes

Buyer Challenges and Outcomes

- ✓ Unable to qualify due to tight credit. In the lower income categories, many of the potential buyers have other financial issues, including credit problems, existing revolving or installment debt payments, and lack of cash for downpayment. As credit markets tighten in response to the current financial crisis, this will become even more challenging, especially for very low income buyers.

- ✓ Unable to qualify due to payment ratios. Home prices are set at the top of the range so families that are otherwise eligible cannot qualify for a loan.

- ✓ Equity not available for repairs or other similar uses. Often a homeowner's primary vehicle for major repairs is refinancing or a homeowner may make improvement to improve the value of their home. While the ordinance allows for some sales price increases based on the value of repairs completed, the buyer is not able to refinance and pull equity out to pay for the repair costs during the time they own the home.

- ✓ Resales are challenging. Like any homeowner, inclusionary owners have life changes, including marriage, divorce, new jobs, etc. that necessitate a move. Many owners have struggled to sell their inclusionary home, as a restricted home cannot compete in our newly affordable market. The ordinance does not allow the option of selling the unit unrestricted or in renting the unit, and some of these buyers have violated their regulatory agreement by selling outside of escrow or renting, and others have lost their homes.

Agency Challenges

- ✓ Need mortgage assistance. Because of the small window for buyers, 36 percent of the inclusionary buyers received additional financial assistance to lower the affordable price even further. As a result, in the 2007 assessment, the average income was 68% AMI. Sources external to the ordinance are required.

- ✓ Properties may decline. While the timeframe is limited, SHRA has concerns that owners have neither the tools nor incentive to maintain or improve their properties. Enforcement mechanisms are limited.

- ✓ Sales and Marketing. SHRA currently advertises available inclusionary homes on our website, and through local counseling groups and lenders. However, some developers have struggled to get sufficient interest in their homes, partly due to the issues already noted, but also because of lack of advertising. Large market rate builders are not always willing to pursue a full marketing campaign for affordable units, and have requested more participation from SHRA in finding qualified buyers. This same challenge exists for either initial sale or resale.