

CITY COUNCIL STUDY SESSION

Multifamily Tax Exemption (MFTE) Program Update

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Community Development Department

DIRECTION NEEDED FROM COUNCIL

DIRECTION

Direct staff on policy questions regarding the MFTE Program Update. In particular, provide direction on the geographic expansion of the program and appropriate balance between the quantity of affordable units and depth of affordability.

RECOMMENDATION

Move to direct staff to develop specific program update language that aligns with staff recommendations regarding the MFTE Update scenario and geographic expansion extent, the interface with land use incentives, addition of a new family-sized unit alternative requirement, and parking inclusion in affordable rent adjustments. Schedule a Public Hearing.

BACKGROUND & ANALYSIS

Program Update Drivers

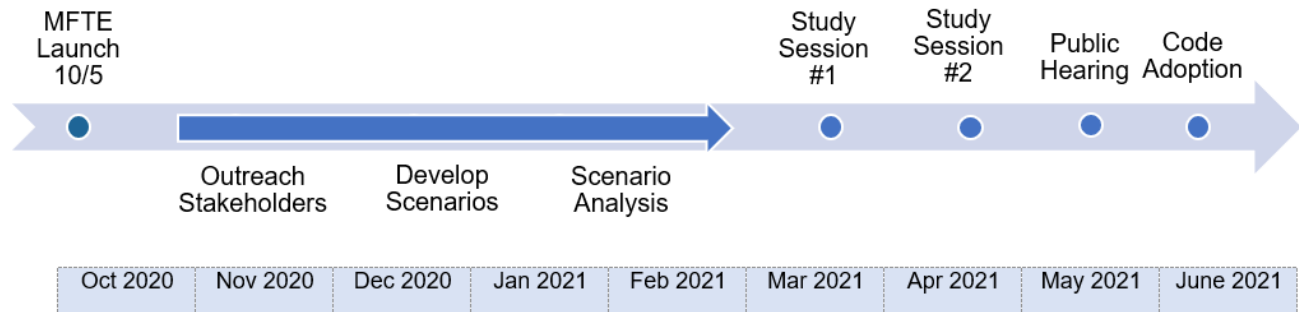
In 2015, the City of Bellevue first adopted the MFTE Program. Based on state law (Chapter 84.14 RCW), this City program allows developers building multifamily housing to gain a 12-year tax exemption on the multifamily improvements in exchange for providing 20 percent of the total number of housing units in the project at affordable rates for a period of 12 years. The current Residential Target Areas (RTAs) where MFTE may be used include the Bellevue growth corridor (Downtown, BelRed, Wilburton) and mixed-use centers of Eastgate and Crossroads.

Council launched an update to the MFTE program on October 5, 2020. The stated goal was to increase utilization of the program in order to increase the availability of affordable housing throughout Bellevue. Two projects totaling 63 affordable units, both in Downtown Bellevue, had utilized MFTE prior to the program update launch. Interest was expressed in both updating the program requirements and increasing the geographic areas where MFTE can be used in the City.

Program Update Schedule

Tonight is the first of two planned Council study sessions on the MFTE Update. Staff plans to return in mid-April with a program update recommendation in response to direction and feedback received from Council. If Council provides specific direction on each policy issue tonight, the second study session could be removed, and the public hearing and code adoption shifted up accordingly. A subsequent Public Hearing would be scheduled based on Council direction prior to code adoption. Since the MFTE

program code lies within the City’s Finance Code (BCC 4.52), Planning Commission review and recommendation is not required.



Current MFTE Program

Bellevue’s MFTE program was adopted as an incentive to incorporate affordable housing in multifamily rental properties being developed in the City. When conceived, it was not intended as a mechanism to make projects feasible that would otherwise have not been feasible. The current program exempts residential improvements from property taxation for 12 years in exchange for setting aside 20 percent of the units for housing affordable to low- or moderate-income households, as follows:

Residential Target Area	Current Program Affordability Levels
Downtown Bellevue	70% of Area Median Income (AMI) for 12 years
BelRed	10% of the units at 50% AMI and 10% of the units at 70% AMI for 12 years
Eastgate, Crossroads Village, Wilburton Commercial Area	10% of the units at 60% AMI and 10% of the units at 70% AMI for 12 years

Affordability levels for the current MFTE program were set on the assumption that projects would also use floor-to-area ratio (FAR) Amenity Incentives, which grant bonus floor area in return for affordable housing priced at 80 percent AMI. The affordable units provided for FAR bonuses (typically less than 10 percent of a project) also count toward the MFTE incentive. Thus, the MFTE program is designed to “buy down” the affordable rents of the FAR incentive program, as well as increase the number of affordable units in a project.

Stakeholder Outreach and Engagement

Following the MFTE Program Update Launch, staff reached out to developers who have either worked on or are currently working on projects eligible for MFTE. In addition, staff have met with members of the Bellevue Downtown Association (BDA) who have expressed interest in affordable housing, including a recent meeting with their newly-formed Housing Task Force. Staff have also met monthly with the Bellevue Chamber’s Permitting, Land Use, Sustainability, and Housing (PLUSH) Committee. Statewide, the MFTE program is generally used by market-rate development projects that use the exemption to offset the cost of offering new units for affordable rents. Therefore, the focus on the

development community has provided valuable insights into the decision process for developers facing the choice of whether or not to use MFTE.

Out of 32 projects that were eligible in the past or are currently eligible for MFTE, staff spoke with or exchanged emails with owners of 21 projects. This was in addition to those who have interacted through other groups such as the BDA or Chamber. The projects that were not assessed were generally either current projects that have gone on pause or part of the Spring District catalyst program, meaning that their affordable housing decision process was altered by unique conditions. Attachment A organizes the comments by topic in relation to the existing program requirements.

The most common reasons for developers choosing not to use the MFTE program fell into three categories. For a few projects, the tax exemption did not cover the rent gap between their planned market rents and the required affordable rents. Those projects were generally higher-end product or did not make use of an FAR land use incentive. Other project owners did not fully understand the MFTE program or were unaware of its ability to overlap with the existing land use incentive for affordable housing. Finally, a few projects found that specific elements of the program were not viable for them, such as the requirement to have 15 percent of the project's units be sized at two bedrooms or larger.

In addition to soliciting feedback on the existing MFTE program, staff also spoke with developers working on current projects that could still apply for MFTE. This allowed staff to examine potential pipeline projects that might use MFTE in the next year or so. Past program utilization was around 15-20 percent, but this is increasing as developers become more familiar with the program and City staff undertake more proactive outreach. Utilization of the MFTE program for 2020-2021 is likely to be closer to 40-50 percent of eligible projects under current regulations. This increased utilization rate includes two MFTE applications totaling 102 affordable units that were approved by the City since the Program Update was launched in October.

Policy Overview

Staff has undertaken significant technical analysis and stakeholder outreach and are now at a point where Council direction relating to policy issues will help staff's ongoing work to develop a comprehensive recommendation for updating the MFTE program. This study session focuses on six topics, each of which is covered in the following sections. The first two topics relate directly to one another, while the others can be taken individually. Staff have provided supporting research and findings alongside their recommendation for each topic below.

1. What level of affordability should be targeted by the program in order to achieve the desired balance between affordability and program utilization?
2. How should the incentives available under the Land Use Code be permitted to overlap with the MFTE program?
3. Should an alternate pathway be permitted for projects that do not meet the current family-sized unit requirement?
4. Should parking be considered a housing cost and therefore incorporated into the affordable rent totals?
5. Should the program be expanded to all Bellevue land use districts that allow multifamily development?

6. Should staff assess an opportunity to provide affordability for the life of the project for MFTE units?

A Balance of Affordability and Quantity of Units

In order to increase access to affordability using the MFTE program, direction from Council is requested on a question central to the program goals. What should the balance be between depth of affordability provided and the quantity of affordable units produced by the program?

Subsidy programs, such as the ARCH Trust Fund, target affordability at 50 percent AMI or lower, though they are permitted to target up to 60 percent AMI. This leaves a gap between 50 percent AMI and the 80 percent AMI targeted by affordable housing land use incentives in Downtown and BelRed. Currently, MFTE is intended to fill this gap. Attachment B highlights the number of affordable units within Bellevue at each AMI bracket, comparing them to the total number of households whose income falls within those brackets. There are more units in the 50-80 percent AMI levels than there are households, meaning that regulated units at those AMI levels generally provide housing for households of lower income. ARCH data supports this, showing that even 80 percent AMI ARCH units provide housing for households of around 55 percent AMI on average. The greatest need for MFTE units is therefore closer to the 50 percent AMI level as opposed to the 80 percent AMI level.

In general, the MFTE program will receive less utilization the deeper the affordability it requires, assuming other factors, such as percent of units required to be affordable, are maintained. The diagram below shows three general scenarios, with sub-scenarios 1A and 1B, and how they fit on the scale between the two. In all scenarios, anticipated utilization of the updated program is expected to exceed the current MFTE program.

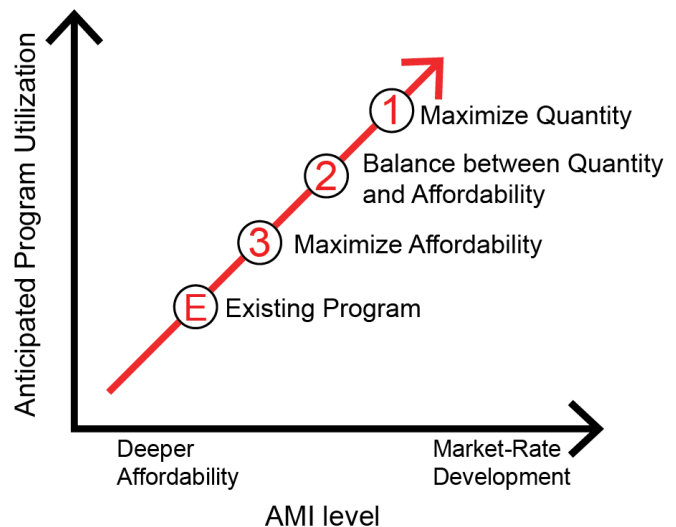
Scenario 1A: Increase utilization as much as possible. Maximize projects using MFTE.

Scenario 1B: Create as many affordable units as possible. Maximize number of units produced.

Scenario 2: Provide a balance between quantity of units and depth of affordability. Focus on having typical projects use the MFTE program. (Staff Recommendation)

Scenario 3: Maximize affordability while also meeting or exceeding the utilization target anticipated by the 2017 Affordable Housing Strategy (65 units per year).

Existing Program: Focus on deeper affordability and on projects utilizing a land use incentive.



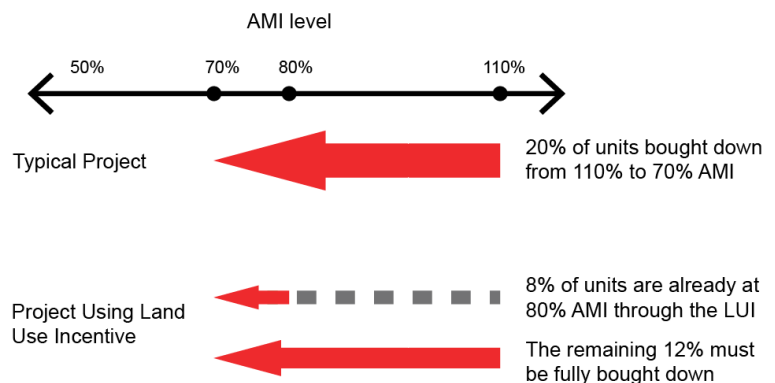
Staff has explored what each of these scenarios might look like and how they might impact developers' decision process. To assist with the analysis, staff developed a financial model with input of the development community that allows testing of a variety of potential program changes. Attachment C explains some of the factors that influence this developer decision process and how anticipated

utilization is evaluated. **Staff requests direction on which scenario or scenarios will achieve the desired balance between affordability levels of MFTE units and the utilization rate of an updated program, so a comprehensive staff recommendation may be brought back for further Council review.** Staff believes that Scenario 3 may not provide the desired program utilization, while either version of Scenario 1 (1A or 1B) may not address the deeper affordability needs that our City faces today. Scenario 2 would provide a good balance between these options and is therefore staff's recommendation for the program update framework.

Interaction with Land Use Incentive Programs

One way to achieve deeper affordability is to allow an overlap between MFTE and the existing affordable housing incentive programs available in the Land Use Code. The diagram below shows what happens with the current MFTE program, which allows for this overlap.

Current Program Example: For a typical MFTE project in Downtown, 20 percent of the units must be affordable at 70 percent AMI. The market is generally around 110 percent AMI today, requiring 40 percent AMI to be bought down by MFTE. If a project chooses to use Downtown's Land Use Incentive for increased density, around 8 percent of units would already be affordable at 80 percent AMI, requiring MFTE to only buy down 10 percent AMI for those units.



MFTE program feasibility is generally higher if the project is also using an affordability housing land use incentive, but it is generally not feasible for projects that do not. Ideally, any MFTE program update would even out the situation to allow for a similar Feasibility Index whether or not a project is using the land use incentive. Attachment D outlines how the scenarios described in this memo could be achieved using a variety of AMI levels and differing approaches to this overlap with the land use incentive.

Related to the scenarios discussed above, staff requests direction on how incentives available under the Land Use Code should be permitted to overlap with the updated MFTE program.

Scenarios 1A and 3 would retain the current regulations, allowing land use incentive units to overlap with MFTE units. Scenario 1B would not allow an overlap at all, while Scenario 2 would allow an overlap but require deeper affordability for those units that are used to satisfy both programs at once. Scenario 2 therefore provides both increased utilization and the ability to offer some units at deeper affordability levels. Staff therefore recommends the approach outlined in Scenario 2.

Family-sized Units

The current MFTE program encourages family-sized unit development by requiring that 15 percent of the total units in the project be two-bedroom units or larger. The housing market generally produces a similar or slightly greater ratio of two-bedroom units, so the development community has not expressed a great issue with this MFTE program requirement. The occasional project may be just below this unit

size requirement and need to choose between adding a few more two-bedroom units in the project or not using MFTE.

There are also occasional projects of a different typology, one that focuses on studios and one-bedrooms. This type of project would not currently be eligible for MFTE, but an update to the program could allow an alternate pathway for these types of projects. For instance, projects that do not meet the 15 percent two-bedroom requirement could be required to offer deeper affordability or a higher quantity of affordable units. Staff have tested these options in the financial model and found them to be viable.

Staff requests direction on whether or not to pursue an alternate pathway for projects that do not meet the current family-sized unit requirement. Staff recommends the addition of an alternate pathway while maintaining the current family-sized requirement as a baseline element of the program. This has the opportunity to increase the utilization rate of the MFTE program in the future by allowing currently ineligible projects to utilize MFTE without losing any family-sized units from the projects that are already eligible.

Parking for Affordable Tenants

Staff requests direction on how the parking needs of affordable tenants should be taken into account in this MFTE program update. The research shows that Bellevue affordable tenants' parking is a necessity in most instances. Any additional parking costs will likely further cost-burden them, so this should be a consideration in any update to the program. There are two basic ways to address this need in the setting of affordable rents. The first would be to offset parking costs for affordable tenants, providing either a discount or an allowance that would partially cover parking. The alternative approach would be to lower the AMI levels of the MFTE units by the amount parking would otherwise cost, likely around 7-8 percent drop in AMI, to lower the overall costs when parking is also considered. Staff recommends the former approach. This allows affordable parking costs to be tied to the presence of transit by linking the parking cost discount or allowance to the code minimum parking requirements for that site.

Geographic Expansion

Council requested an expansion to the areas where MFTE may be used, the Residential Target Areas (RTAs). In particular, a focus on areas with access to frequent transit was requested. Attachment F overlays the frequent transit network (locations with four or more stops per hour) with Bellevue's multifamily or mixed-use zoning. The shaded region represents a half-mile buffer from each transit stop. This area covers nearly all of the zones in which multifamily development is permitted. Staff therefore recommends that the program be expanded to all zones that permit multifamily development. While most development has been occurring in the existing RTAs, this would allow flexibility for future projects outside these areas to use the MFTE program. **Staff requests direction regarding expansion of the MFTE program to all Bellevue land use districts that allow multifamily development.**

Life of Project Affordability

As part of their analysis, staff have looked into increasing the required affordability from 12 years to the life of the project. While other complicating factors may need to be incorporated into any further analysis, this change would result in an increase in the AMI affordability level by about 15-20 percent in

order to achieve similar program utilization. This would push affordability levels too high in the case of a 12-year program, but it could potentially be incorporated into a new eight-year program with a requirement for around 8 percent of units to be affordable for the life of the project. Council could direct staff to further evaluate this option if desired. **Staff requests direction on whether or not to further evaluate this option as part of the MFTE program update.**

Project Administration

Council requested that staff evaluate the current administrative procedures for unnecessary or unclear requirements that could be a burden to projects pursuing use of the program. These administrative procedures were discussed with stakeholders and found to be acceptable as they currently function. Stakeholders requested that clarity be provided on the City website and MFTE materials so that requirements such as unit distribution throughout the building are made clear from the start. As part of this program update, staff will therefore review all public-facing documents and ensure clarity on the administrative process.

POLICY & FISCAL IMPACTS

Policy Impact

A shift in the MFTE program will likely result in a different quantity and affordability level of units produced through the program. More units would likely mean less deep affordability, which requires a policy change. Part of this policy discussion is influenced by the ability to overlap the program with affordability incentives available in the Land Use Code.

In addition, policy decisions regarding the inclusion of family-sized units, inclusion of parking within the affordable rent, geographic expansion, and the exploration of life-of-project affordability are required.

Fiscal Impact

Increased utilization of the program would result in an increased number of tax exemptions. These represent taxes that would have been collected on the new residential construction had the project been constructed without utilizing the MFTE program. The tax exemption is not entirely foregone, as part of it is sometimes shifted to other taxpayers. Attachment G explains this variation and its impact on the City and other taxpayers.

OPTIONS

1. Direct staff to develop specific program update language that aligns with staff recommendations regarding the MFTE Update scenario and geographic expansion extent, the interface with land use incentives, addition of a new family-sized unit alternative requirement, and parking inclusion in affordable rent adjustments. Schedule a Public Hearing.
2. Direct staff towards a specific MFTE Update scenario and geographic expansion extent, and provide feedback on program elements including interface with land use incentives, mix of family-sized units, parking inclusion in affordable rent, and/or length of MFTE affordability. This will inform staff's ongoing work to develop a comprehensive recommendation for updating the MFTE program. Schedule additional study session to review.
3. Provide alternate direction to staff on the MFTE Program Update.

ATTACHMENTS & AVAILABLE DOCUMENTS

- A. Existing MFTE Program: Outreach Comments
- B. Affordable Housing Gaps
- C. Financial Model Description and Risk Factors
- D. MFTE Update Scenarios Chart: Preliminary Findings
- E. Affordable Housing: Parking Demand
- F. 2020 MFTE Evaluation: Potential Expansion Opportunities
- G. Fiscal Impact

AVAILABLE IN COUNCIL LIBRARY

Bellevue Affordable Housing Strategy, June 5, 2017