C. C. 106

City of Cambridge

MASSACHUSETTS

In City Council May 20 1991

C. Cyr — Referred to Finance Committee

Re: Agenda H-4

	YEA	NAY	ABSENT	PRESENT	
Mr. Ed Cyr	✓				
Mr. Francis H. Duehay	✓				
Mr. Jonathan S. Myers	✓				
Mr. Kenneth E. Reeves	✓				
Mrs. Sheila T. Russell		✓			
Mr. Walter J. Sullivan		✓			
Mr. Timothy J. Toomey, Jr.	✓				
Mr. William H. Walsh		✓			
Mayor Alice K. Wolf	✓				
	6	3			

CAMBRIDGE AFFORDABLE HOUSING PROGRAMS
BASIC EVALUATION CRITERIA
MAY, 1987

EQUITABLE
- Mechanism must be equitable

IMPLEMENTABLE
- Mechanism must be politically implementable

LEGAL
- Mechanism must be legally defenseable

ECONOMIC
- Mechanism must allow for economic feasibility

FLEXIBLE
- Mechanism must allow for flexibility in the method of contribution

PREDICTABLE
- Mechanism must allow participants to predict contributions

ADAPTABLE
- Mechanism structure must adapt to changing markets

EFFECTIVE
- Mechanism sucess must be measurable

MANAGABLE
- Mechanism must be practical to administer and enforce

ADJUSTABLE
- Mechanism must allow for adjustment in response to evaluation

Transfer Tax

Equitable - Of all of the mechanisms which we have tested, transfer taxes spread the responsibility for affordable housing among the broadest possible base of constituencies. In particular, the transfer tax mechanism most affectively acknowledges the idea that new development is not solely responsible for affordable housing shortages within the City. A transfer tax mechanism is indeed the most equitable means of sharing the responsibility for affordable housing production within the City of Cambridge.

Implementable - As previously described, political feasibility will be essential to the City's ability to implement any one of the techniques described by this analysis. In our judgement, given that transfer taxes would equitably distribute the responsibility for affordable housing production we judge that this mechanism in turn provides the greatest likelihood for generating broad based political support. Indeed, the notion of political feasibility could be further enhanced through the adoption of a system to exempt small scale transactions from the calculation. In this way, moderately priced residential units might be removed from a transfer tax system without adversely affecting the notion of maintaining equity while yet maximizing the effectiveness of the program in generating revenues to achieve affordable housing objectives.

Legal - A transfer tax system could only be adopted through a successful legislative approvals process. There are several bills pending now before the State Legislature and there is a reasonable likelihood that an acceptable bill can be crafted and approved through a concerted and thoughtful negotiation and lobbying effort. Perhaps the greatest drawback to the a successful adoption of the transfer tax method is the time needed to secure legislative approval. We would recommend, however, that despite the timing issues the long term benefits of a transfer tax program far outweigh the near term concern that new development projects now in the planning stages might escape the affordable housing process. Indeed, if a transfer tax mechanism can be instituted, the ability to raise funds for affordable housing will not be solely dependant upon new projects and thus the need to capture the revenue generation potential represented by these new projects becomes far less critical to the achievement of program objectives.

Economic - An analysis of the economic impacts of transfer taxes on the development economics of a wide variety of project scales and types reveals that a transfer tax payment of 1% of transaction value could be levied in the market place without unduely affecting development feasibility within the City of Cambridge. Indeed, at a 1% rate no project regardless of size or use, new or existing, residential or commercial, good location or bad location would be rendered infeasible. Our tests of market impacts included an examination of transfer taxes of 2% and 3%. At these higher rates, development feasibility across the board can only be achieved with a system of substantial exemptions. In our judgement, it makes both economic and public policy sense to minimize the reliance on exemptions systems and to construct the appropriate formulas on the basis of an understanding of the lowest common denominators.

Aside from the issues of economic feasibility, perhaps one of the most attractive characteristics of a transfer tax mechanism from an economic prospective involves the notion that because participation would be broadly distributed, individual contributions would be very low. In this way, no project or person or business would be dramatically impacted.

Flexible - We have described the need for flexibility in terms of providing market participants with the option to either contribute cash, unit production, land donations, resident occupancy write-downs, etc. Under a transfer tax method this kind of built-in flexibility becomes a moot point. The dollars which the City can generate from the transfer tax can be used to fund housing production, to buy land, to write-down occupancy, or better still, to leverage additional funds. So, while the capital production mechanisms itself is not flexible, the City would enjoy a maximum of flexibility in determining the uses of funds generated.

Predictable - A transfer tax provides the most predictable means for gaging the extent of participation in an affordable housing program. The rates would be established. They would be known in advance. And all market participants would have an ability to adapt their individual plans to meet the transfer tax requirements.

Adaptable - Of all of the mechanisms examined, the transfer tax mechanism because it is based on changes in market value is most effective in self adjusting to the dynamic to the market place. Coupled with the fact that individual contributions would be low because anticipated market participation would be high, the transfer tax method is likely to be least suceptible to unexpected downturns in the market. As such, it holds the greatest potential for ensuring development feasibility and economic health over the long term.

Effective - Again, because of the anticipated broad participation in a transfer tax system this method of fund raising produces the greatest potential for revenue production. In addition, because it is transaction-based rather than founded in new development projects, the certainty and security of annual revenue streams far exceeds that produced by any other method examined. Indeed, assuming that the transfer tax rate were set at only 1% of sale value and assuming that the first $300,000 of every transaction were exempted from the calculation, this method would yet produce secure revenues of $2 million per year to support affordable housing programs.

Manageable - A transfer tax mechanism could be implemented through existing tax revenue collections procedures. Since the participation in this kind of program would be strictly formulaic, there would be no need for extensive review or negotiation processes to establish the participation requirements for any individual project. As with all mechanisms which we have tested, the real management intensity for this method would be a function of how best to allocate the funds collected.

Adjustable - The transfer tax mechanism could be adjusted on an annual basis as part of existing tax rate review processes. Once adopted, these review procedures should be reasonably easy to implement.

CAMBRIDGE LINKAGE COMMITTEE
COMPARISON OF KEY CRITERIA
MAY, 1987

GENERIC AFFORDABLE HOUSING PRODUCTION STRATEGIES

BASIC TESTS		TRANSFER TAX	LINKAGE EXACTION	INCENTIVE ZONING	VOLUNTARY CONTRACTS
EQUITABLE	PROS	o Spreads responsibility among broad base of constituencies which impact housing availability and affordability	o Places responsibility on developers and occupants of new projects which impact housing affordability and availability	o Places responsibility on developers and occupants of new projects but provides zoning or permitting relief in exchange	o Places responsibility on developers and occupants new projects
	CONS	o May miss interests transfered by trusts or through leases	o Ignores existing development projects as well as all others contributing to the affordable housing shortage	o Ignores existing development projects as well as all others contributing to the affordable housing shortage	o Ignores existing development projects as well as all others contributing to the affordable housing shortage
RANKING :		1	4	2	3

CONCLUSION : The transfer tax mechanism most effectively acknowledges the idea that new development alone is not solely responsible for affordable housing shortag
Of options examined, a transfer tax mechanism is therefore the most equitable in spreading responsibility for affordable housing production.

BASIC TESTS		TRANSFER TAX	LINKAGE EXACTION	INCENTIVE ZONING	VOLUNTARY CONTRACTS
IMPLEMENTABLE	PROS	o More palatable to broad based constituencies given equitable distribution of responsibility provided that some form of exemption is provided for moderate value residential units	o More palatable to resident and existing business constituencies given limited distribution of responsibility	o More palatable to development constituencies given incentive provide for compliance and ability to develop by right	o More palatable to development constituencies given voluntary nature of contribution
	CONS	o Less palatable to resident and existing business constituencies given broad distribution of responsibility	o Less palatable to development constituencies given limited distribution of responsibility	o Less palatable to resident constituencies given potential for modification of zoning requirements	o Less palatable to resident constituencies given voluntary nature of contribution
RANKING :		1	4	2	3

CONCLUSION : A transfer tax mechanism provides the broadest base of support for implementation provided that homeowner exemptions are instituted.
Incentive zoning provides another reasonable approach to garnering broad support given that developers receive something in return for participation.
Voluntary mechanisms are apt to experience problems given their lack of certainty.
Linkage exactions are least likely to be palatable with the development community given that nothing is given in return for participation.

Leggat McCall Advisors, Inc.

GENERIC AFFORDABLE HOUSING PRODUCTION STRATEGIES

BASIC TESTS		TRANSFER TAX	LINKAGE EXACTION	INCENTIVE ZONING	VOLUNTARY CONTRACTS
LEGAL	PROS	o Once enacted will be less susceptable to legal challenge	o Once enacted will be less susceptable to legal challenge	o Can be enacted under existing zoning ordinance and can thus can be implemented quickly	o Can be enacted through policy directive and can thus be implemented quickly
	CONS	o Requires state legislative approval before enactment and will thus take more time and energy to implement	o Requires state legislative approval before enactment and will thus take more time and energy to implement	o If enacted through existing zoning, will be susceptable to legal challenge	o Legal challenges may yet arise in response to claims of inconsistency or unfairness in negotiation of contributions
RANKING :		1	3	1	2
CONCLUSION :		A transfer tax if enacted will be least susceptable to challenge. Incentive zoning provides a means for expedient implementation. Voluntary contributions while easy to implement from a legal perspective yet leave the City open to challenge Linkage exactions are both lengthy to implement and likely to yet result in legal challenge			
MANAGABLE	PROS	o Could be managed and enforced through existing revenue collection procedures	o Number of cases to be reviewed will be low given limited distribution of responsibility	o Number of cases to be reviewed will be low given limited distribution of responsibility	o Number of cases to be reviewed will be low given limited distribution of responsibility
	CONS	o Number of cases to be reviewed will be high given broad distribution of responsibility	o Will create significant added work for existing departments and boards or will require the creation of a new department	o Will create significant added work for existing departments and boards or will require the creation of a new department	o Will create significant added work for existing departments and boards or will require the creation of a new department
RANKING :		1	1	1	1
CONCLUSION :		Each method will require significant organizational structure to ensure that contributions are both collected and applied to housing production goals			
ECONOMIC	PROS	o Individual contributions will be very low given broad distribution of responsibility	o Approach to establishing a linkage fee gives priority to economic issues	o Ability to develop by right provides for assurance of economic feasibility	o Voluntary nature of method provides for assurances of economic feasibility
	CONS	o Must be carefully dovetailed with existing tax policy so as not to stifle economic activity	o Must be carefully dovetailed with existing tax, zoning, and development approvals policies so as not to stifle economic activity	o Must be carefully dovetailed with existing tax, zoning, and development approvals policies so as not to stifle economic activity	o In a highly competitive climate developers may be tempted to agree to more than can reasonably be provided economically
RANKING :		1	4	2	3
CONCLUSION :		A transfer tax mechanism provides the best assurance of economic feasibility in given that the absolute payments are low and that they are self adjusting to the market. Incentive zoning also provides reasonable assurance of economic feasibility in that developers yet have the option to develop by right or receive something in return. Voluntary mechanisms assure feasibility but at the expense of other objectives Linkage exactions are least effective in assuring economic feasibility given that they do not adapt readily to changing markets			

Leggat McCall Advisors, Inc.

GENERIC AFFORDABLE HOUSING PRODUCTION STRATEGIES

BASIC TESTS		TRANSFER TAX	LINKAGE EXACTION	INCLUSIONARY ZONING	VOLUNTARY CONTRACTS
FLEXIBLE	PROS	o While not flexible, a tax provides a high level of predictability in both the amount and method of payment	o Can be structured to be highly predictable yet offer options for unit production, land donation or cash contributions	o Can be structured to be highly predictable yet offer options for unit production, land donation or cash contributions	o Voluntary nature of method provides for assurances of flexibility
	CONS	o A tax offers no flexibility beyond the potential to vary the payment term	o Will require strong mechanism for converting cash and land donations into housing	o Will require strong mechanism for converting cash and land donations into housing	o Will require strong mechanism for converting cash and land donations into housing
RANKING :		1	1	1	1
CONCLUSION :		Each method provides significant opportunity for flexibility			
ADAPTABLE	PROS	o Self adjusts to changing market conditions	o Approach to establishing a linkage fee gives priority to economic issues	o Ability to develop by right provides for some assurance of market adaptability	o Voluntary nature of method provides for adaptation in changing markets
	CONS	o Must be carefully dovetailed with existing tax policy so as not to stifle economic activity	o Not self-adjusting for changing market conditions	o Not fully self-adjusting for changing market conditions	o Contributions are not predictable or guarenteed should markets weaken
RANKING :		1	4	2	3
CONCLUSION :		A transfer tax mechanism provides the best assurance of economic feasibility in given that the absolute payments are low and that they are self adjusting to the market. Incentive zoning also provides reasonable assurance of economic feasibility in that developers yet have the option to develop by right or receive something in return. Voluntary mechanisms assure adaptability but at the expense of other objectives Linkage exactions are least effective in assuring economic feasibility given that they do not adapt readily to changing markets			
EFFECTIVE	PROS	o Existing revenue collection procedures allow for easy measurement of collections	o Number of cases to be measured will be low given limited distribution of responsibility	o Number of cases to be measured will be low given limited distribution of responsibility	o Number of cases to be reviewed will be low given limited distribution of responsibility
	CONS	o Method for measuring the effectiveness of programs for converting collections into housing for must be developed	o Method for measuring the effectiveness of housing production programs must be developed	o Method for measuring the effectiveness of housing production programs and zoning impacts must be developed	o Method for measuring the effectiveness of housing production programs and zoning impacts must be developed
RANKING :		1	1	1	1
CONCLUSION :		Each method will require significant organizational structure to ensure that contributions are both collected and applied to housing production goals			

GENERIC AFFORDABLE HOUSING PRODUCTION STRATEGIES

BASIC TESTS		TRANSFER TAX	LINKAGE EXACTION	INCLUSIONARY ZONING	VOLUNTARY CONTRACTS
ADJUSTABLE	PROS	o Can be reviewed annually as part of existing revenue review and adjustment process	o Can be reviewed periodically as part of an established review and adjustment process	o Can be reviewed periodically as part of an established review and adjustment process	o Self-adjusts to changing market conditions
	CONS	o Modifications except those which deal with reduction or repeal of requirements will be difficult to implement	o Modifications except those which deal with reduction or repeal of requirements will be difficult to implement	Modifications will likely have to include changes to both contributions methods and base line zoning regulations	o Does not self-adjust to changing housing needs
RANKING :		1	1	1	1

CONCLUSION : Each method will require significant organizational structure to ensure that a system for periodic review and modification is instituted.

	TRANSFER TAX	LINKAGE EXACTION	INCLUSIONARY ZONING	VOLUNTARY CONTRACTS
TOTALS	9	21	13	17
% OF PERFORMANCE SCALE	100 %	53 %	85 %	69 %

NOTES: ON A SCALE OF 9 TO 36 : 9 IS BEST - 36 IS WORST

CITY OF CAMBRIDGE
COMMUNITY DEVELOPMENT DEPARTMENT
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4.

May 16, 1991

To the Honorable, the City Council:

RE: Council Order #22, dated 12/10/90, Re: Real Estate Transfer Impact Fee

In 1987, the Community Development Department (CDD) commissioned a study, prepared by Leggat McCall, entitled "Cambridge Affordable Housing, Legislative and Regulatory Capital Formation Mechanisms." Leggat McCall was asked to analyze different methods for raising capital to support affordable housing production programs. The study reviewed and made recommendations related to four different regulatory and legislative methods of capital formation - transfer tax, linkage exaction, incentive zoning and voluntary contracts. Based, in part, on this report's recommendation the Cambridge City Council in July 1988 enacted the current Incentive Zoning requirement. Incentive Zoning was a mechanism that could be approved on a local basis and did not require the City to gain State approval. Since the initial adoption of Incentive Zoning, the Council has requested State Home Rule authority to extend the linkage requirement to as-of-right commercial development.

The report identified the transfer tax mechanism as "the method [which] constitutes the best means for raising funds to support affordable housing in the City of Cambridge." The criteria used to judge the methods included economic feasibility in different market conditions, quantity and security of income, simplicity of administration and equity in terms of distributing responsibility for affordable housing over the broadest base. The portions of the report which evaluate the transfer tax according to these and other criteria are attached. The strongest drawback to adoption of the transfer tax was the necessity of State Home Rule enabling legislation prior to Council enactment. Similar types of enabling legislation as well as State-wide authorization have been defeated in the Legislature.

Leggat McCall, after reviewing different feasibility models, recommended that the transfer tax be set at one percent of sales and that the first $300,000 of any sale be exempted from the tax. The one percent fee did not render any project infeasible while a higher rate of tax might negatively impact development feasibility particularly of smaller projects.

If the one percent transfer tax had been applied to sales in the past year (Dec.'89 - Dec.'90) with the first $300,000 of any sale exempted, approximately $474,000 would have been raised. If the exemption was more limited, that is sales up to $300,000 were exempted, but the full amount of sales over $300,000 were taxed, then approximately $939,800 would have been raised. The sales figures are based on both residential and commercial sales.

An additional exemption which the Council may wish to consider is the exemption of first-time homebuyers although exempting sales under $300,000 would likely cover most of these purchasers.

Yours truly,

Robert W. Healy

Robert W. Healy
City Manager

RWH:SS:nb

CONSENT AGENDA # 4 S-718

Awaiting Report Item Number 6 regarding
the development of a real estate
transfer impact fee.

In City Council,

May 20, 1991

Referred to the
Finance Committee
6-3-0.

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