

# The Santa Clara Model:

A market-based approach to affordable home ownership

**A Presentation to the California Chapter of the American Planning Association**

**Monday, October 1, 2007**

**San Jose Fairmont Hotel**

**Regent Room**

**3:00-4:15 pm**

**Kevin L. Riley & Jeffrey Pedersen**

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# The Panel

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- Moderator

Kevin Riley, Director of Planning & Inspection  
City of Santa Clara

- Homebuilder

Charles McKeag, Vice President of Acquisition & Development  
Citation Homes Central

- Community Lender

Jonel Jackson, Regional Builder Manager  
First Horizon Home Loans

- Non-profit Developer & Lender

Edward Moncrief, Executive Director  
Neighborhood Housing Services, Silicon Valley

- City Housing Administrator

Jeffrey Pedersen, Housing & Community Services Manager  
City of Santa Clara



# The Topic

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Inclusionary zoning has been championed by advocates as a means to ensure that the American Dream of homeownership doesn't disappear for hardworking Californians. Truly, a "House is more than a Home" because the challenge is balancing an equitable approach for all stakeholders: the Homebuyer, the Developer, the Mortgage Lender, and the City.



# Why Santa Clara cares about Affordable Housing?

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## The Policy Basis :

- State Regional Housing Needs Allocation (RHNA) mandates production of “fair share” housing for all income levels in a community (*Government Code Sections 65583 & 65584*)
- City cares about its residents and has an adopted Community Goal of “Maintaining a strong commitment to affordable housing” and providing for the needs of the community
- General Plan Housing Element has a 10% Inclusionary Policy requirement for new development (10+ units) or condominium conversions
  - Rental projects required to provide 10% of units at rents affordable to lower-income households
  - For-Sale projects to provide 10% of units affordable to moderate income households



# Santa Clara's Perspectives

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- Housing Need (i.e. "The Demand for Housing") is a broad continuum that is influenced by socio-economic factors and market forces that cannot be easily satisfied by a "one-size-fits-all" solution:
  - Not Everyone is capable of, or should be a Homeowner
  - It's OK to be a Renter
  - Special Needs Populations  
(e.g. Homeless, Developmental Disabled, Transitional Populations)
- Santa Clara's approach is to provide a spectrum of housing choices



# Santa Clara's Perspectives

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- Housing Stock is Dynamic and the City will always be faced with the basic questions of "Where and How will people live?"
  - Everyone wants to live in safe, decent housing w/ a good quality of life
  - The City's Housing Production is on-going and will not stop at the end of the General Plan or Housing Element cycles
  - In-fill, Re-fill, and Redevelopment projects prove that the term "Built Out" is really just another way to say N.I.M.B.Y.
  - Santa Clara plans for the needs of its residents & businesses both present and future.



# Santa Clara's Perspectives

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The only tools available to local cities to assist in affordable housing production:

1. Land Use Entitlements (Rezoning, Subdivision, Density Bonus)  
Approval of private development projects w/ Conditions of Approval requiring provision of affordable housing units
2. Financial Assistance (RDA, CDBG, & HOME, etc.)  
-Below-market loans to Developers & Buyers in exchange for affordability restrictions



# Home Builders' Perspectives

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- Land use policies must be EFFICIENT and FAIR if they are to be EFFECTIVE.
- MOST INCLUSIONARY ZONING POLICIES ARE INEFFECTIVE because they fail to address the needs of homebuyers, the realities of the marketplace, and the legitimate business concerns of homebuilders.
- THE SANTA CLARA BMP PROGRAM IS EFFECTIVE because it provides maximum value to homebuyers, minimizes the subsidy burden on homebuilders, and creates a mechanism for generating additional subsidy dollars for future affordable housing efforts.





# Home Builders' Perspectives

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- Every project must be financially viable to justify taking on the economic and legal risks associated with building homes

## **No Project = No Units**

- Each project requires a significant up-front investment of time, energy, and money, and profits are never guaranteed
- Each project presents unique challenges that cannot be addressed by "one size fits all" regulatory constraints
  - Relationship of Project to Community's Housing Needs
  - Consideration of Alternative Housing Types (same bdrm count)
  - Consideration of In-Lieu Fees
  - Consideration of Off-Site Units



# Home Builders' Perspectives

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- What makes Santa Clara's BMP Program EFFICIENT?
  - Low Cost + High Value = Timely Delivery of Product
  - Implementation responsibility is left to Affordable Housing experts – not forced on market-rate builders
  - Program works with the market, not against it
- What makes Santa Clara's Program FAIR?
  - Subsidy cost is shared between public and private sectors
  - Seeks to limit impact on homebuilder profits and avoids the “punitive” aspects common to most inclusionary programs
  - Allows buyers to participate in the investment process instead of relegating them to permanent “second-tier” status



# Home Builders' Perspectives

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- EFFICIENCY + FAIRNESS = EFFECTIVENESS

- Homebuilders are allowed to run their business without the added risks and burdens associated with the production of costly but unmarketable affordable product.

- Homebuyers making “moderate” incomes are given an opportunity to participate in the real estate market – and potentially climb the economic ladder – without being burdened with onerous resale restrictions.

- The City ensures a consistent stream of new affordable homes by generating revenue from its participation in the equity build-up of its existing affordable stock. This revenue can then be invested in a variety of affordable housing projects and programs that may produce units at lower price levels than the primary BMP program.



# Lenders' Perspectives

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- Financial Institutions review Federal and State Regulations, Secondary Market Requirements (e.g. Fannie Mae or Investor expectations), and analyze risk when deciding whether or not to make loans:
  - Most Lenders Will Sell Their Loans on the Secondary Market
  - Anything that detracts from ability to resell loan will discourage lenders from making a loan
  - Loan Underwriters consider “Worst-case” Scenarios with the ideal goal that the Promissory Note holder is always in “First Position” then paid upon default.
  - Lenders’ Expect Secondary Loans & Affordability Covenants to be subordinate to their Loans w/ only a limited cure period



# Lenders' Perspectives

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- Affordability Restrictions Effect the Ability to Finance and Sell Units:  
**NO Mortgage Loans = NO Unit Sales**
  - Lenders will always want to be in “First Position” and only subject to very limited cure provisions upon a buyer’s default
  - Rigid Affordability Covenants will ensure that potential lower-income buyers will not be able to get affordable financing
  - Lenders will only provide Written Notifications required by Federal or State Regulators or the Secondary Market
  - Local Program requirements may constrain available buyer financing (e.g. Only Fixed Rate Loans, Percentage of Gross Income Req.)



# Lenders' Perspectives

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- Affordability Covenants alone are not adequate to protect the long-term affordability of “restricted” units:
  - Most Title Companies, Real Estate Agents, and Lenders Do Not Pay Attention to Unsecured Recordings
  - Often Confused with CC&R's for Homeowners Associations
  - Buyer Amnesia
  - Unauthorized Loans or Over Financing
  - Unauthorized Sales or Rentals
  - Performance best secured by a Deed of Trust on Title



# Lenders' Perspectives

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- City must be aware of Federal, State & Secondary Market Lending Regulations (e.g. FANNIE MAE, RESPA, HMDA, etc.)
- Importance of Buyer Education and Disclosure
- Federal & State House Hold Income Limits and Definitions Drive Affordability Formulas and Sales Prices



# Buyers' Perspectives

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- What is the Housing Market in Silicon Valley Today?

New Single Family List Prices: \$665,900-\$774,900

Existing Single Family Resale Price: \$778,000 (Median)

Approx. Monthly Mortgage Payment: \$4,700

New Condominium List Prices: \$300,000-\$559,950

Existing Condo Resale Price: \$493,400 (Median)

Approx. Monthly Mortgage Payment: \$3,160

Typical County Monthly Mortgage Payment: \$3,048

(HOA, taxes, insurance, utilities and maintenance add \$500 - \$800)





# Buyers' Perspectives

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- The Current Barriers to First Time Homeownership
  - High Sales Prices even with growing inventory
  - Tightening Credit Market and More Conservative Lending Practices
  - Lack of Knowledge About Homebuying Process
  - Poor or No Credit History
  - Lack of \$\$\$ for Down Payment or Closing Costs
  - Lack of Market Knowledge - **“Is this a Good Time to Buy?”**

Shaped by Buyer Confidence & The Media



# Buyers' Perspectives

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- The Psychology of Purchasing the “American Dream” Now Includes a Strong Expectation for the Home to Be a Good Long-Term Investment
  - Buyers Expect Equity & Positive Benefit from Homeownership

**No Equity = No Sales**

- Buyers Becoming Savvy to Downside of Long Term Restrictions

**“Isn’t that Just a Glorified Rental Unit?”**

- Effect of HUD Median Income Freeze - “Hold Harmless” Provision

Income Limits Drive Future Sales Prices

**The possibility of No Equity – Ever ???**



# Buyers' Perspectives

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- Disclosure and First Time Homebuyer Education are Critical:
  - Buyers Must Understand their the Sale & Financing Transactions (“What is The Deal”)  
**“I don’t remember how I bought a \$500k unit for \$300k?”**
  - Buyers Potentially Trapped by Increasing Ancillary Housing Costs (i.e. HOA, taxes, insurances, maintenance, etc.)  
**\$1,200 Mortgage Payment & \$ 2,000 new HOA assessment**
  - Added Responsibilities of Homeownership  
**No Landlord to Call for Repairs**



# Buyers' Perspectives

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- What is Neighborhood Housing Services Silicon Valley (NHSSV)?
  - Non-profit housing corporation providing products & services to low- and moderate-income FTHB's
    - i) Non-profit Lender (CALHFA Approved)
  - Santa Clara's Administrative Partner for its BMP & FTHB Programs
    - i) Administrative Services for BMP Program (Including Monitoring)
    - ii) Homebuyer Education and Credit Counseling
    - iii) Pre-Qualification for Financing & City Program Criteria
    - iv) Marketing of BMP Units
    - v) Buyers' Agent during Sales & Escrow Process



# Santa Clara Model

## Home Ownership Programs

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- Redevelopment Agency

First Time Home Buyers Financing Program (FTHB)

- City of Santa Clara

Below Market Price Purchase Program (BMP)



# Santa Clara Model

## Home Ownership Programs

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- RDA First Time Home Buyers Financing Program
  - Available for all for-sale homes in Santa Clara
  - 120% AMI Eligibility
  - Available through City approved lenders
  - CalHFA approved
  - 3% Downpayment Required
  - Provides a 20-year, \$75,000 Secondary Mortgage Loan
  - No interest or payments for 1<sup>st</sup> 5-yrs
  - Fixed simple interest at primary loan rate after 5-yrs



# Santa Clara Model

## Home Ownership Programs

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- City Below Market Purchase (BMP) Program
  - Inclusionary Policy requires 10% of units in new for-sale housing developments w/10+ units to be affordable (includes condo conversions)
  - Affordable Housing Agreement (AHA) with Developer secures implementation of BMP provisions.
  - Units are priced at a Moderate Income Affordability Level (100% of AMI)
  - Allows RDA First Time Homebuyer Financing Program



# Santa Clara Model

## Home Ownership Programs

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- City Below Market Purchase (BMP) Program
  - Deed of Trust secures Promissory Note capturing City entitlement value of inclusionary unit
  - Covenant secures performance on Resale Restrictions
  - Request for Notice Recorded





# Santa Clara Model

## Home Ownership Programs

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- City Below Market Purchase (BMP) Program
  - 20-year Affordability/Resale Restriction allows market resale after 5 years of ownership.
  - Homeowners are able to participate in the same housing economy as market-rate owners after owning for 5 years.
  - If homeowners decide to sell unit w/in the first 5 years, BMP unit must be sold to qualified, income-eligible homebuyer at restricted affordable sales price.



# Santa Clara Model

## Home Ownership Programs

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- Below Market Purchase (BMP) Program Definitions
  - City appraisal sets Initial Market Value (IMV) prior to the initial sale based on the Unrestricted Market Value of the unit w/o the affordability restriction in place.
  - For each BMP unit in a project, the City establishes an Affordable Sales Price (ASP).
  - The difference between IMV & ASP is the value of the inclusionary requirement, the principle of the City loan, (amount that the homebuyer owes the City if the home is resold at an unrestricted resale price after 5 years.



# Santa Clara Model

## Home Ownership Programs

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- City Below Market Purchase (BMP) Program
  - Homeowners share of any appreciation increases by 5% per year for 20 years.
  - Equal equity appreciation as market-rate homeowners is available after 20 years of ownership.



# Santa Clara Model

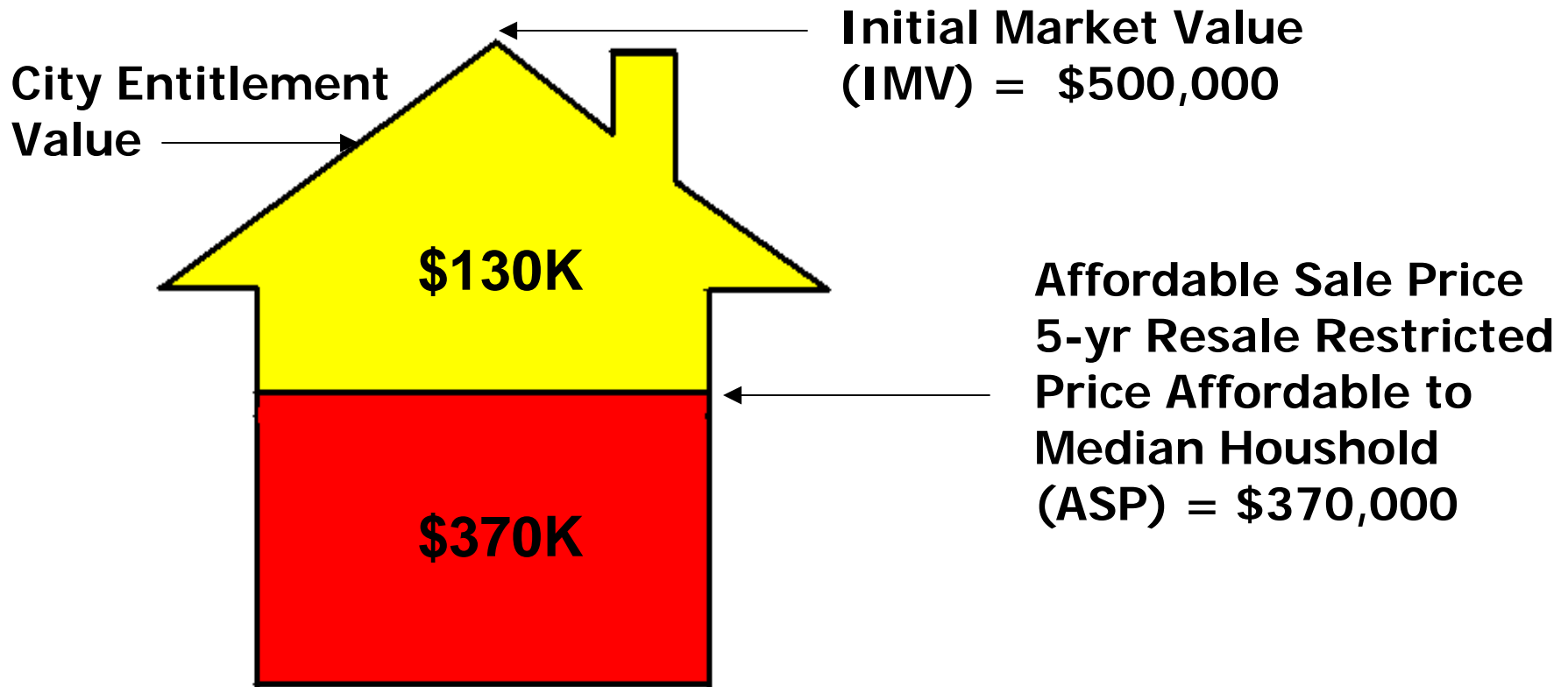
## Home Ownership Programs

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- City Below Market Purchase (BMP) Program
  - Financially qualified buyers – no waiting list.
  - Priority given to City residents and employees.
  - Sales contract w/buyer notes the ASP but also the IMV.
  - ASP is used in calculating property taxes.
  - Buyers complete Buyer Acknowledgement Forms w/ the individual details of their purchase (full disclosure).
  - Buyers must pass a separate test to be given opportunity to purchase a BMP unit.

# Santa Clara Model

## Home Ownership Programs

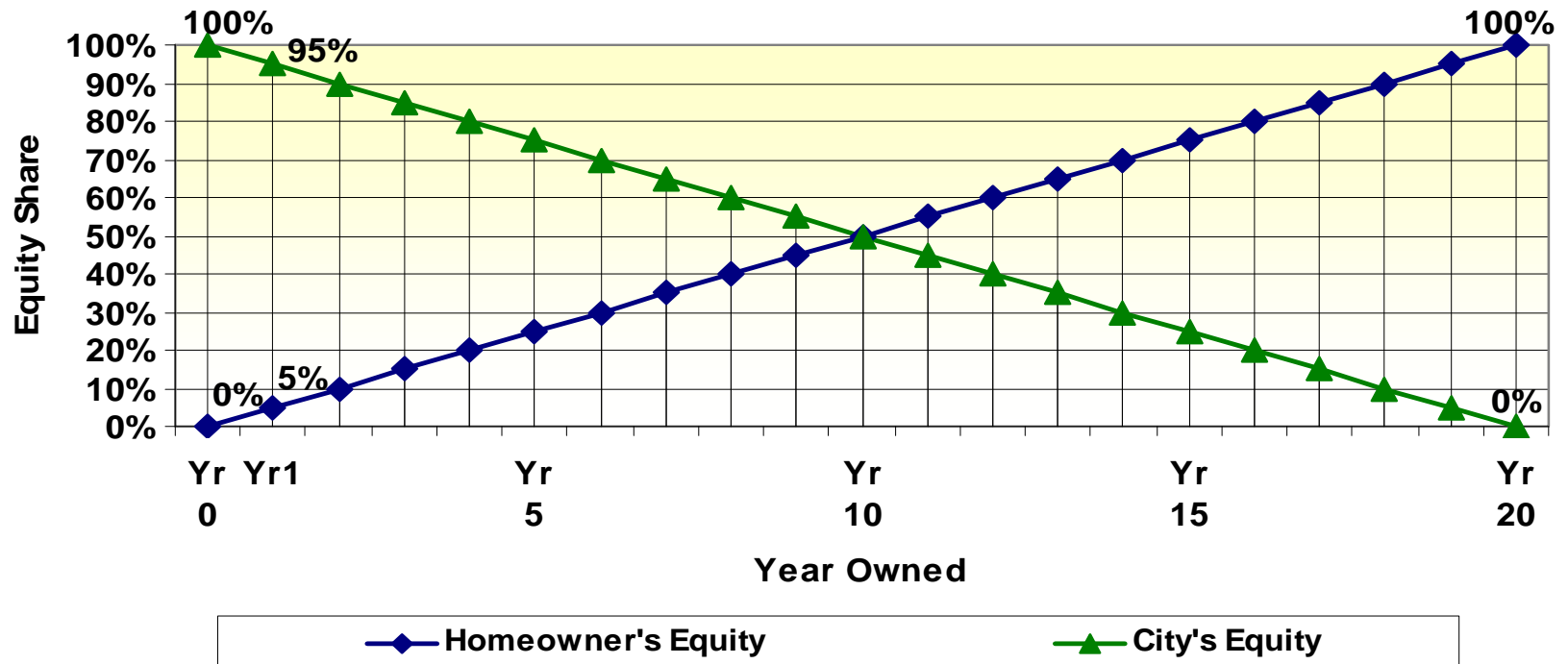


**IMV and ASP Illustrated**

# Santa Clara Model

## Home Ownership Programs

### Market Approach for Equity Gain

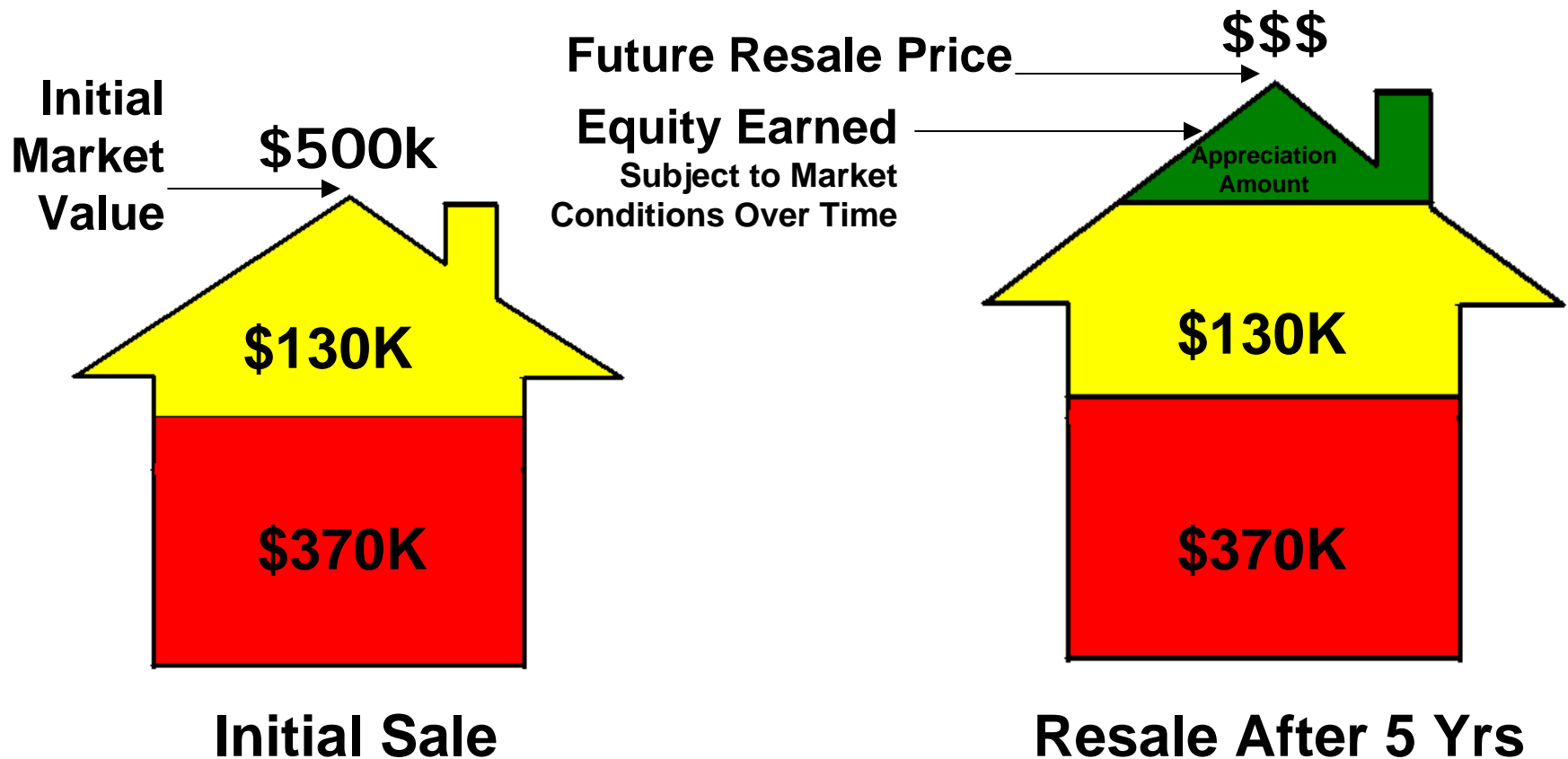


The longer a unit is owned, the larger the share of equity gained. After 20 years, Homeowners gets all the equity above the IMV.

# Santa Clara Model

## Home Ownership Programs

### Market Approach for Equity Gain





# Santa Clara Model Home Ownership Programs

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## **BMP Program 6 Month Summary** March thru August 2007

### **Development/Units Info**

9 Housing Projects w/ 41 Sales

### **Future Revenue Info**

\$2.7 M payable in RDA FTHB Loans  
\$5.0 M payable in City BMP Loans

### **Typical Client Info**

BMP Unit Type:	2-Bedroom Condominium
Initial Market Value:	\$500,000
Affordable Sales Price:	\$370,000
Avg. Household Size:	2.3 Persons
Annual Household Income:	\$80,465 (84.7% of AMI 3-person HH)
Avg. Down-payment:	\$32,044 (8.7% of Aff. Sales Price)





# Santa Clara Model

## Home Ownership Programs

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### Typical BMP Financing

#### Loans:

CalHFA 1 <sup>st</sup> Mortgage	\$ 249,000
HiCAP	\$ 7,500
RDA-FTHB	\$ 75,000
HTSCC	\$ 6,500
Down Payment	<u>\$ 32,000</u>
Total Purchase	\$370,000

City Note	\$130,000
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#### Monthly Expenses:

Principal/Interest	\$ 1,200
Property Taxes	\$ 320
HOA/Insurance	\$ 300
PMI	<u>\$ 0</u>
Total Payment	\$1,820

SCC 2-Bdrm Avg. Rent	\$1,826
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# Advantages/Benefits Santa Clara BMP Program

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- Recognizes: City as the producer of affordable housing through entitlement process.
- Recognizes: Redevelopment Agency as a method of mortgage financing.
- Requires a 5-year residence and incentive to own BMP unit long term.
- Allows the local housing market economy to influence BMP owners similar to market-rate owners.
- Enables a BMP household to improve their socio-economic standing by accessing market equity appreciation that is equal to their neighbors.



# Advantages/Benefits Santa Clara BMP Program

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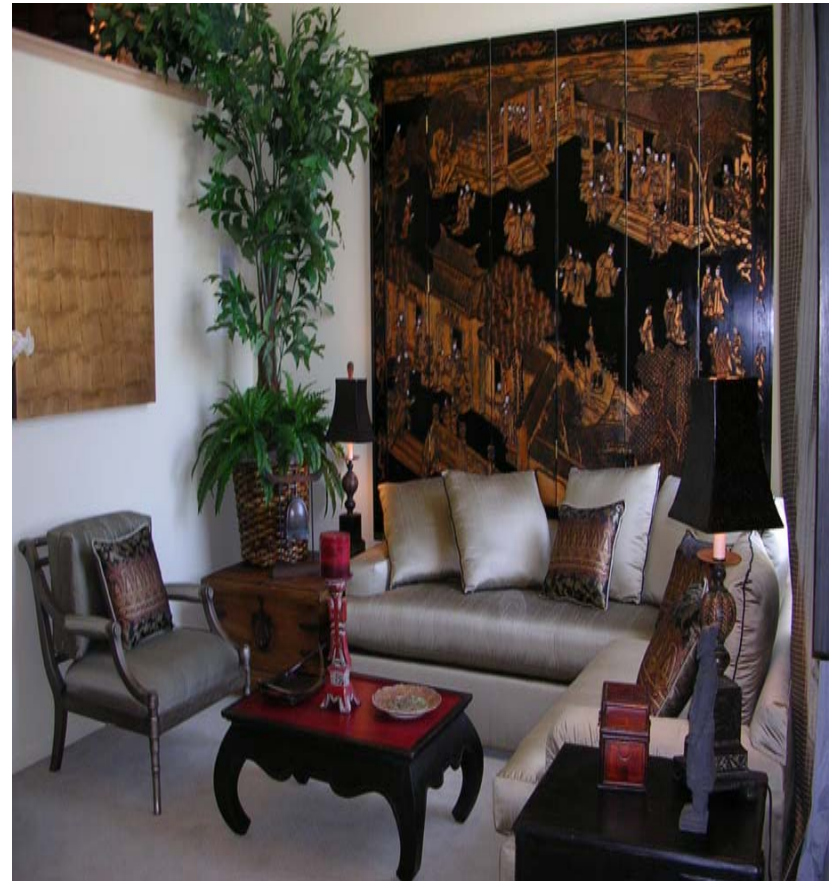
- Promotes a BMP owner's future ability to enter the free market for home ownership.
- Creates an incentive that encourages investment and better home maintenance of BMP units.
- Results in a simplified relationship between the City & the Developer and the City & the homebuyer.
- Reduces the City and Agency long-term administrative burden for monitoring compliance to the use restrictions:
  - Annual Loan Notices to Buyer (Obligation Reminder).
  - City provided Notice of Sale or Refinance.
- Provides a funding resource for the City to meet its future housing needs.

# Santa Clara Model Home Ownership Programs



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# Santa Clara Model Home Ownership Programs

