



## **Chapter 3 Pricing and Sale of Ownership/For-Sale Inclusionary Units - Section 18.27.20(C)**

### **1. Pricing of For-Sale Inclusionary Units**

For-Sale Inclusionary Units are sold at below market prices by taking the difference between Fair Market Value of the home and the Affordable Sales Price, an adjusted Affordable Housing Cost, as described later in these Guidelines. The buyer of an Inclusionary Unit acknowledges the Affordable Sales Price provided under the Ordinance by executing Subordinate Shared Appreciation Loan documents and agrees to the income restriction and other conditions. In escrow, the buyer executes a City promissory note and other Subordinate Shared Appreciation Loan documents that reflect this cost differential.

"Fair Market Value," for the purposes of the Ordinance and the Guidelines, means the highest price on the date of valuation that would be agreed to by a seller, being willing to sell but under no particular or urgent necessity for so doing, nor obligated to sell, and a buyer, being ready, willing and able to buy but under no particular or urgent necessity for so doing, each dealing with the other with full knowledge of all the uses and purposes for which the Inclusionary Unit is reasonably adaptable and available but as though there was no affordability requirement imposed on the home. The Fair Market Value shall be verified by a licensed real estate appraiser, commissioned by the borrower or borrower's lender, prior to the close of escrow.

The Developer must provide 90 days' advance written notice to the City of the initial marketing of the Inclusionary Units. The Housing Division will calculate the Affordable Housing Cost, as adjusted to an Affordable Sales Price pursuant to these Guidelines, which will then be identified as the maximum affordable price that may be charged to prospective homebuyers for the Inclusionary Unit within a Residential Development. This calculation of Affordable Sales Price shall be done within 90 days before the date of the first close of escrow for an Inclusionary Unit in a Residential Development and the values (Affordable Sales Price and Fair Market Value) shall be updated every 90 days thereafter.

#### Method of Calculating the Income Limit for Pricing

First, using the number of bedrooms in the particular Inclusionary Unit, the maximum income limit is adjusted for household size. Income limits are published by the City of East Palo Alto on its website on an annual basis. As defined in Health and Safety Code Section 50052.5 (h), household size is equal to one person greater than the number of bedrooms in the unit. Specifically, for the purpose of determining the income limit in order to calculate the Affordable Housing Cost, each Inclusionary Unit shall be adjusted for household size appropriate for the unit based on the number of bedrooms as follows: a studio = one person, one bedroom = two persons, two bedrooms = three persons, three bedrooms = four persons, and four bedrooms = five persons.



### Method of Calculating the Affordable Housing Cost and Affordable Sales Price

The Affordable Housing Cost shall not exceed 30% of the Income Limit. The monthly Affordable Housing Cost is calculated by dividing the Affordable Housing Cost by 12. This monthly Affordable Housing Cost is intended to cover all of the purchaser's housing costs; therefore, in order to determine the maximum Affordable Sales Price, that Affordable Housing Cost amount must be adjusted as described below.

To determine the Affordable Sales Price from the monthly Affordable Housing Cost involves a three-step process:

1.) Subtract applicable property taxes, homeowners' association fees, annual maintenance and repair allowance, insurance – including hazard insurance, mortgage insurance and other applicable insurance – and utilities cost from the monthly Affordable Housing Cost amount. The remainder is the amount that would be available to pay the monthly mortgage payment (monthly Affordable Mortgage Payment).

The Housing Division will use the following criteria to calculate housing related expenses that must be covered by the Affordable Housing Cost in addition to the mortgage payment:

- i. **Homeowner Association (HOA) Fees** – Actual amount approved by the State of California Department of Real Estate for the project.
- ii. **Property Tax** – The Housing Division will use the standard of 1.2% of the market price of the unit. In the event that any special assessments bring the property tax rate above 1.2%, the City will utilize the actual property tax rate for the Inclusionary Unit.
- iii. **Utility Costs** – Derived from Utility Allowance schedule provided by the San Mateo County Housing Authority. The utility allowance must include heating, cooking, other electric, water heater, water, and garbage, if not included in HOA fees. The utility allowance changes periodically so please [check the website](#) to obtain current information.
- iv. **Hazard Insurance Cost** – If not included in HOA fees, the City will estimate the monthly cost of hazard insurance at \$100. This amount may be adjusted for inflation.
- v. **Mortgage Insurance Premium** – If the calculated amount of the cost differential between the Affordable Sales Price and the Fair Market Value is not greater than 20% of the Fair Market Value of the property, the Housing Division will establish a market rate Private Mortgage Insurance (PMI) premium corresponding to the rates published by the Federal Housing Administration (FHA).
- vi. **Maintenance and Repair Allowance** of \$25 per bedroom, per month. This amount may be adjusted for inflation.



2.) Follow the process below to calculate the amount of the mortgage loan that could be obtained (Financed Affordable Loan) based on the amount of monthly Affordable Mortgage Payment as determined in Step 1 above.

- i. The mortgage loan interest rate shall be based on a 5% down payment, thirty (30) year, fully amortizing fixed rate mortgage based on the Freddie Mac Weekly Mortgage Survey at the time of pricing, as determined by the Housing Division. This mortgage amount does not include any pre-paid points or loan fees.
- ii. Use the monthly Affordable Mortgage Payment, the interest rate calculated above, and a fully amortized fixed rate mortgage without points or loan fees to determine the maximum Financed Affordable Loan.

3) Add to the Financed Affordable Loan amount determined in Step 2 an assumed amount of borrowers' own funds of 5% for a down payment to determine the Affordable Sales Price.

## **IX. Homeowner Inclusionary Housing Requirements**

The Developer (or designee) is responsible for the screening and qualification of the initial purchaser of a For-Sale Inclusionary Unit as outlined in detail below and for incorporating any applicable Local Preference guidelines for the selection of households into the screening process. Local Preference guidelines shall be provided in a separate document.

### **1. Household Composition Definition**

The Household is comprised of all eligible individuals who are currently living together at the same address and will continue to be living together in the Inclusionary Unit.

New household members cannot be added to the application to income qualify for an Inclusionary Unit after initial submission of an application. In addition, the following individuals are not counted as part of the household: foster children, unborn children, children who are subject to a shared-custody agreement, in which the child resides with the household less than 50% of the time, children being pursued for legal custody or adoption who are not yet living with the household at the time of application, and non-related live-in care-takers.

To be considered an Eligible Household Member, an individual must comply with the above criteria and meet one of the following criteria:

- i. Individuals 18 years of age or more (adult household members). Adult household members must be included for income qualification purposes and must appear on the application to purchase the Inclusionary Unit; or



- ii. Any minor individual who is a dependent listed on the most recent year's tax returns of an adult household member. All household members who are under 18 years of age must be the legal dependent of an adult household member.

## 2. Household Income Limits for Buyers

To establish the eligibility of households who intend to occupy the Inclusionary Unit, limits are set on the amount of income households (which includes all Eligible Household Members) can earn. These limits are based on the area median income (AMI) and the number of Eligible Household Members.

The Ordinance requires that Inclusionary Units be sold to Median- and Moderate-Income Households, as defined below:

- 1.) Median-Income Households: households whose income does not exceed 80 percent of the area median income, adjusted for family size and as published annually by the City;
- 2.) Moderate-Income Households: households whose income does not exceed 120 percent of the area median income, adjusted for family size and as published annually by the City.

The City of East Palo Alto will annually provide this information on its website.

## 3. Household Income Definition

Households shall not have an income in excess of 80% or 120% of AMI (Household Income Limit). The family size to be used for determining the Household Income Limit is the number of Eligible Household Members.

For income eligibility purposes, the gross annual income (income before deductions or exemptions) received by all Eligible Household Members 18 years of age or older will be considered. The gross annual income is determined by calculating the Household's total current monthly income and then multiplying that total by 12. In the event that current monthly income deviates by more than 15% from the preceding 12-month average, the gross annual income will be determined by combining the preceding half year's gross income with one-half year's gross income at the current level.

## 4. Types of Income

- i. All wages and salaries, overtime pay, commissions, fees, tips, bonuses, and other compensation for personal services, before payroll deductions;



- ii. The net income from the operation of a business or profession or from the rental of real or personal property (without deducting expenditures for business expansion or amortization of capital indebtedness, or any allowance for depreciation of capital assets);
- iii. Interest and dividends (including income from assets – see Excluded Income section below)
- iv. The full amount of periodic payments received from Social Security, annuities, insurance policies, retirement funds, pensions, disability or death benefits, and other similar types of periodic receipts, including any lump sum payment for the delayed start of a periodic payment;
- v. Payments in lieu of earnings, such as unemployment, disability compensation, and severance pay;
- vi. The maximum amount of public assistance available to household members, other than the amount of assistance specifically designated for shelter and utilities;
- vii. Periodic and determinable allowances, such as alimony and child support payments, and regular contributions or gifts received from persons not residing in the home;
- viii. All regular pay, special pay, and allowances of a member of the Armed Forces (whether or not living in the dwelling) who is the head of household or spouse; and
- ix. Any earned income tax credit to the extent that it exceeds income tax liability.

#### 5. Excluded Income

- i. Casual, sporadic or irregular gifts;
- ii. Amounts that are specifically for, or in reimbursement of, medical expenses
- iii. Lump sum additions to household assets (as defined in the Assets section below), such as inheritances, insurance payments (including payments under health and accident insurance and workmen's compensation), capital gains, and settlement for personal losses;
- iv. Monies received for educational scholarships paid either directly to students, or to the educational institution, as well as amounts paid by the Government to a Veteran of the U.S. Armed Forces for use in meeting the costs of tuition,



fees, books, and equipment. Any money received over and above the associated educational costs listed are not exempt and considered income;

- v. Special pay to a person in the U.S. Armed Forces who is head of household who is deployed and exposed to hostile fire;
- vi. Foster child care payments;
- vii. The value of benefits received from the Supplemental Nutrition Assistance Program;
- viii. Payments to volunteers under the Domestic Volunteer Service Act of 1973;
- ix. Income derived from certain sub-marginal land of the United States that is held in trust for certain Indian tribes;
- x. Payments or allowances made under the Department of Health and Human Services' Low-Income Home Energy Assistance Program; and
- xi. Payments received from the Job Training Partnership Act.

#### 6. Determination of Income from Assets

To determine a Household's income eligibility for purchase of an Inclusionary Unit, a percentage of the Household's assets (as defined in the Assets section below) shall be added to the Household income only when the total of the Household's assets exceeds the annual Household Income Limit. The amount of income attributed to these assets shall be computed as the higher of:

- i. The actual annual income generated from the assets; or
- ii. 2.5% of all assets in excess of the Household Income Limit.

#### 7. Assets

Assets are defined as:

- i. Cash savings, including but not limited to bank accounts, credit union accounts, certificates of deposit, and money market funds;
- ii. Marketable securities, stocks, bonds, and other forms of capital investment;
- iii. Inheritance and lump sum insurance payments already received;
- iv. Settlements for personal or property damage already received;



- v. Equity in non-residential real estate such as commercial property and unimproved land, except as described as “not considered asset” below; and
- vi. Other personal property that is readily convertible into cash.

The following are not considered assets:

- i. Ordinary household effects including furniture, fixtures, and personal property;
  - ii. Automobiles used for personal use;
  - iii. Any deposits on Inclusionary Unit (Equity on a parcel or lot on which an Inclusionary Unit is to be built); and
  - iv. Cash, securities, stocks, bonds, and other forms of capital held in a tax deferred retirement plan recognized by the Federal Internal Revenue Service.
8. Execution of Subordinate Shared Appreciation Loan Documents; Restrictions

Each purchaser shall be required to execute a promissory note in favor of the City East Palo Alto, secured by a deed of trust for the amount of the Subordinate Shared Appreciation Loan. The City shall also require a recorded Affordability Restriction as described in Part IX, Section 9 below and may require execution of a loan agreement and other ancillary documents. The Subordinate Shared Appreciation Loan amount is the difference, if any, between the restricted Affordable Sales Price of the Inclusionary Unit and its Fair Market Value at the time of the initial sale to the purchaser.

If the property is subsequently transferred to a non-qualified affordable buyer, the Subordinate Shared Appreciation Loan would become due and payable along with a prorated percentage of any equity received in the sale to a non-qualifying buyer under the Ordinance. The Subordinate Shared Appreciation Loan would not become due and payable if the property is sold to a qualified buyer under the Ordinance who agrees to assume the loan, in an arm’s length transaction. If the property is sold to a qualified buyer under the Ordinance who does not agree to assume the loan, then the Subordinate Shared Appreciation Loan would become due and payable along with a prorated percentage of any equity based on the then Fair Market Value of the unit.

The Inclusionary Unit shall be the purchaser’s primary place of residence. To be considered as a principal place of residency, the Inclusionary Unit must not be rented or leased unless the purchaser has a household hardship and has applied for and obtained an emergency limited term authorization to rent approved by the Housing Division. In the event that the purchaser fails to comply with this





requirement, the City may enforce and pursue any and all remedies in law or equity for such violations, including, but not limited to, declaring the Subordinate Shared Appreciation Loan due and payable.

Upon request of the Housing Division, the purchaser of the Inclusionary Unit must provide, within 30 days, documents verifying the purchaser's occupancy of the home as the purchaser's primary residence, that the home is not rented or leased, and that there have been no changes in the title to the home. Such documents may include but are not limited to utility bills, property tax bills, and mortgage statements reflecting the owners name and address of the Inclusionary Unit. Pursuant to the Subordinate Shared Appreciation Loan documents, an annual submittal will be required thereafter, along with a monitoring fee.

9. Execution of an Affordability Restriction

Each purchaser of an Inclusionary Unit shall be required to execute and consent to recording of an Affordability Restriction in perpetuity for their unit at close of escrow. The restriction will be recorded and "run with the land" such that it is binding on any successor to the purchaser. The Affordability Restriction shall require that the purchaser occupying the home as a principal residence, unless a hardship exception is granted. It shall also require that any sale of the Inclusionary Unit be limited to sale to a new qualified affordable purchaser at an Affordable Sales Price, and that any request to sell to a non-qualified buyer must be approved by the City.