



County of Santa Cruz

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REDEVELOPMENT AGENCY

701 OCEAN STREET, ROOM 510, SANTA CRUZ, CA 95060-4000

(831) 454-2280 FAX: (831) 454-3420 TDD: (831) 454-2123

TOM BURNS, AGENCY ADMINISTRATOR

May 8, 2001

Agenda June 5, 2001

Board of Directors
County of Santa Cruz Redevelopment Agency
701 Ocean Street
Santa Cruz, CA 95060

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First Time Home Buyer Program

Dear Members of the Board:

During the past few years, accelerating home prices have placed home ownership out of reach of most potential first-time home buyers who work in Santa Cruz County. At the current median home price of about \$461,000, a family would need to accumulate a down payment of approximately \$50,000 (10% down) and have an household annual income of at least \$115,000 in order to afford the typical house. Contrast these figures to the typical wages for service jobs in our County and one can see how truly out-of-reach home ownership has become for most families working in Santa Cruz County.

Back in 1996, the Redevelopment Agency established a First Time Home Buyer Program to assist lower income households in home purchases. That program initially worked well, but unfortunately, as the real estate market surged the past several years, it has become ineffective.

With the growing community-wide concern about the ability of our local workforce to access the housing market, staff has in the past several months reviewed a wide range of options for reshaping the First Time Home Buyer Program to once again be an effective tool to assist qualifying households in home purchases. This report reviews those proposed changes, which are directed toward the needs of households with incomes shown below.

California EDD date (March 2000) indicates the following annual salary by job type in Santa Cruz County: teacher - \$43,680, police officer - \$51,730, fire fighter - \$42,960, nurse - \$31,510, loan officer - \$44,940, physical therapist - \$67,900, sales clerk - \$21,210, medical secretary - \$26,050, electrician - \$38,300, plumber - \$40,860.

Background

In April 1996, your Board authorized Agency staff to implement a First Time Home Buyer Program. The program was designed to assist low income families with the purchase of their first home by providing a "silent second" loan of up to \$25,000 which could be used for cash down payment and closing costs. Payment on these loans was deferred for five years, after which time payments would begin assuming the household's income had increased to a level where it could support additional debt service. To preserve potential affordability of the unit, the Agency would record an option agreement intended to restrict the resale price in the event of a rapidly increasing real estate market. During the past four years, the Agency has assisted 42 low income households with loans totaling almost one million dollars, although most of the households were assisted in the early years of the program.

The housing market has changed dramatically since the beginning of the program in 1996. Since 1996, the County's median home sales price has increased 92% while County median household income has increased only 19%. In 1996, the County's median home sales price was \$240,000 - about 4.3 times the 1996 County median income level of \$56,000. Today, the median home sales price is about \$461,000 - about 7.0 times the current County median income level of \$65,500. Stated another way, in 1996 34% of the County's households could afford a median priced home, while today only 16% of the County's households can afford a median priced home. As a result, few, if any, homes are priced within the purchasing power of lower income households, even with substantial down payment assistance through the Agency's program. The home purchasing dilemma facing low income families has now expanded to include moderate income families.

Overview of Proposed Program Changes

In response to the evolving market conditions, a number of changes to the current First Time Home Buyer Program are recommended at this time. Those changes include the following:

- ▶ raising income limits from low income to moderate and increasing the program assistance loan limit from \$25,000 to \$50,000 to increase families' purchasing power;
- ▶ expanding the program to include the purchase of manufactured homes in mobile home parks for lower income households;
- ▶ strengthening and clarifying the program goal of creating long term affordable units; and
- ▶ requiring that purchasers of these units work in Santa Cruz County.

A more detailed summary of the proposed changes is provided in Attachment 1.

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Program Limitations

To make this program viable for low and moderate income households in today's housing market, it is proposed that the maximum purchase price for a single family home be \$288,200. This is the maximum price a moderate income eligible household can afford, given the State law requiring no more than 35% of income be used to cover housing costs, and assuming a maximum Agency loan of \$50,000. For mobile homes, utilizing similar assumptions for low income households with a maximum Agency loan of \$20,000, the maximum purchase price of a mobile home would be \$94,000. Even with these proposed changes, the program will only be available for a limited number of home purchase opportunities. Under current State law, the only way to expand the program's reach would be to increase the per unit Agency subsidy amount. Staff does not believe that such an increase is justified, given the per unit level of subsidy required for other existing housing programs. Please be assured that Agency staff will carefully monitor this program and it is recommended that your Board be provided with a status report on or before April 9, 2002.

It is worth noting that your Board has taken a position in support of Senator McPherson's proposed bill (SB 459) which, if adopted, would increase the maximum housing cost ratios of these programs - currently restricted to 35% of income - to the level commonly used by lending institutions of 40% of income. Passage of this Bill would increase the current maximum unit sales price from \$288,200 to \$330,900, expanding the inventory of homes eligible for the Agency's Program. Your Board previously has taken a position supporting this Bill. If it becomes law, staff will then make changes to the program in accordance with the provisions of this law.

Summary and Recommendation

The recommendations in this letter, and described in greater detail in Attachment 1, address the proposed changes to the Agency's First Time Home Buyer Program to provide a meaningful and pragmatic response to overwhelming housing market changes. The program's proposed changes reflect a continued commitment to address the housing need for low income home buyers while expanding benefits to include moderate income home buyers. The program is similar to programs throughout the Monterey and San Francisco Bay Areas, in that the program would formally focus on serving our local workforce, an essential factor contributing to the future economic vitality of our community. While the program changes recommended will not solve the local housing affordability crisis, they will certainly provide much-needed opportunities for home ownership for low and moderate income families.

Once approved by your Board, it will take four to six weeks to put the proposed program changes into effect, including time for **FannieMae** and **FreddieMac** to approve our revised

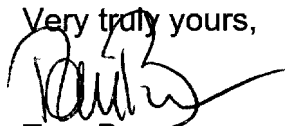
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program documents and for Agency staff to prepare new guidelines and outreach materials. Financing of \$500,000 is provided in the proposed FY 2001-02 Agency Budget for this program.

It is therefore RECOMMENDED that your Board, as the Board of Directors for the Redevelopment Agency, take the following actions:

1. Approve the changes to the Agency's First Time Home Buyer Program, as outlined in this report;
2. Authorize the RDA Administrator to take all actions necessary to implement this program; and
3. Direct the RDA Administrator to provide a status report on the program's effectiveness on or before April 9, 2002.

Very truly yours,




Tom Burns

Redevelopment Agency Administrator

TB:rmcb

RECOMMENDED:



Susan A. Mauriello

Redevelopment Agency Director

Attachment

cc. RDA

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**Recommended Changes to the
Santa Cruz County Redevelopment Agency
First Time Home Buyer Program Guidelines**

To address changes in the local real estate market, provide housing affordability for both low and moderate income home purchasers who work in Santa Cruz County, and ensure that assisted units remain affordable for future purchasers, the following program changes are recommended:

	Existing Program	Recommended Program Changes	
		Real Property SFD, Condo, Townhouse or PUD	Manufactured Home in Mobile Home Park
Unit Type	Units secured by underlying real property (cannot be mobile home)	Same as existing	Would become eligible for low income households
Income Limit	80% of County median income	110% of County median income	80% of County median income
Funding Type	5-year deferred loan; with subsequent payments based on increased income	Transferable shared appreciation loan	Transferable shared appreciation loan
Maximum funding	\$25,000 or 15% of purchase price	\$50,000 or 15% of purchase price	\$20,000 or 15% of purchase price
Affordability Restriction	Secured by option agreement where Agency must acquire/assign option to new buyer	Secured by long term affordability covenant	Secured by long term affordability covenant
Use of funds	Cash down payment and closing costs	Cash down payment	Cash down payment
Maximum purchase price	Effectively, none	110% of County median income for 4 person household times 4 (currently \$288,200)	80% of County median income for 4 person household times 1.8 (currently \$94,000)
Workforce requirement	None	Work in Santa Cruz County	Work in Santa Cruz County

Raise income limits from low income to moderate and increase program assistance loan limits from \$25,000 to \$50,000 to increase families' purchasing power.

Although a critical need is still manifested by lower income households, households in the moderate income category also have been dramatically affected by accelerating housing prices. It is therefore recommended to raise eligible income levels from 80% to 110% of County median household income. This means that current income eligibility for the program for a household of four would be increased from \$52,400 to include households which earn up to \$72,050 annually. Additionally, greater purchasing power can be realized by increasing the program assistance limit from the current limit of \$25,000 to \$50,000. Increasing the Agency's First Time Home Buyer Program's eligible income levels and assistance limit will increase the

program's potential home purchase price from \$175,000 to \$288,200, dramatically expanding potential program participation. A review of actual sales in the unincorporated county area during the 13-month period between January, 2000 and February, 2001 shows that only 20 homes were sold at a price of \$175,000 or less while 191 homes sold at \$288,200 or less.

Expand the program to include the purchase of manufactured homes in mobile home parks for lower income households.

As noted above, due to escalating home prices, it is no longer possible to focus the program solely for traditional home purchase by lower income families. Instead, staffs evaluation of home prices found that the best home purchase opportunities for lower income households are within existing mobile home parks. At a median price of \$98,000, manufactured homes in mobile home parks remain the lowest priced home ownership alternative in the County. Within the recommended maximum purchase price of \$94,000, a family of four can reasonably afford to purchase one of these units, but in most cases, would be unable to save the full down payment. Through the Agency providing down payment assistance, these units would become accessible for lower income families. A review of actual sales in the unincorporated county area during the 13-month period between January, 2000 and February, 2001 shows that 50 homes sold in this price range.

Strengthen and clarify the Program goal of creating long term affordable units.

Some aspects of the current Program should be changed to ease administration and clarify its purpose. Under the current process, affordability is retained through the Agency exercising its option to purchase upon resale. Under this approach, the loan to the Agency is paid off by the home seller and the unit is sold to another low income household, typically with the Agency issuing another First Time Home Buyer loan to the new purchaser. This approach required extensive Agency involvement in each transaction and created potential confusion among program participants about the on-going role of the Agency in the sale and resale of units. To ease program administration and remove the Agency from its role as an intermediary yet maintain long term unit affordability, it is proposed that the program be structured to allow Agency loans to be transferred from sellers to buyers.

Shifting the Agency's assistance from repayable loans, that get an individual household into a one-time affordable housing situation, to shared appreciation loans that can be transferred from sellers to buyers will clarify the program's long term goal. When shared appreciation loans are paid off by sellers, the loan proceeds (which equal 15% of the sale/purchase price) may be applied toward the buyer's cash down payment. A transferrable loan balance of this type will clarify the program's main purpose which is to provide adequate down payment assistance loans for future income qualified first time home buyers, without further Agency subsidies.

While the proposed resale procedures allow homeowners to sell their homes themselves with little Agency involvement, the Agency would inspect units, determine their maximum resale price, verify household eligibility and ensure appropriate resale restrictions were carried forward to each new purchaser. In order to preserve affordability in the event a program participant defaults on their loan, the Agency would have a purchase option at the restricted price which would be exercised only upon default by borrowers, or upon request by owners who have not successfully marketed their units.

Finally, by providing a more substantial subsidy of up to \$50,000 to make these units affordable with a per unit subsidy amount that is commensurate with other Agency assisted for-sale or rent restricted projects, it is consistent with State law that the Agency restrict units purchased through this program with long term affordability covenants.

Set an initial maximum home purchase price at a level which, when allowed to increase at the same pace as area median income, will ensure affordability to the next purchasers of the unit.

In order to ensure that homes purchased through this program are affordable to future buyers, maximum initial home sales prices would be established commensurate with annual changes in the County's median income levels. Initial home prices would be set based on State law which encourages Redevelopment Agencies to provide housing at "affordable housing cost." Under the State's current definition, households pay no more than 30% - 35% of their income for debt service, taxes, insurance and utilities costs. Given reasonable assumptions for mortgage rates and housing costs, the formula for determining maximum purchase prices can be calculated by multiplying median incomes (for targeted four person households) by a factor of 4 for conventional homes, and a factor of 1.8 for manufactured homes. Purchase prices for mobile homes would be set at a lower relative level to take into account higher mortgage interest rates, shorter term loans and the additional burden of space rents. This technique directly links County household incomes, affordable housing costs and home price levels.

Require that purchasers of homes work in Santa Cruz County.

While the recommended First Time Home Buyer Program is proposed to expand to include moderate income households, it is suggested that it be focused on housing for our local work force, and that as a prerequisite participants be employed in Santa Cruz County. This focus will ensure that the local workers who qualify for this program have an opportunity to be homeowners here. Furthermore, this policy is consistent with other high cost communities in our area who provide similar home buyer opportunities. The program will be designed for marketing to major employee groups, including local school districts, public agencies and service providers. With a large segment of the County's workforce composed of government and institutional workers, including key community service personnel (police officers, firefighters,

nurses and teachers), this program could expand the local community's ability to retain and attract much-needed employees. This approach will provide numerous benefits for our local workforce, employers and the community.

Proposed formula for determining the resale price and Agency loan repayment amounts

According to our proposed formula, the resale price of the home is equal to the original purchase price of the home as increased by the percentage increase in area median income (AMI). This amount may be further adjusted by the value of any capital improvements. In addition, the repayment amount of the Agency loan is equal to the original principal amount of the Agency loan as increased by the same percentage increase in AMI. As you can see from the below example, because both the resale price and the Agency's "shared appreciation" loan increase at the same rate, the original financing structure remains the same from buyer to buyer. Therefore, the ability to purchase the home with only 5% cash down payment, and affordable monthly housing costs, is assured for all future moderate income home buyers.

Example of possible purchase and sale transactions

The following chart illustrates the possible long term effect of the recommended program changes after two sales. The chart assumes that area median income (AMI) continues to increase by the historical average of about 6% a year. In an upward market, the program's structure allows owners to sell their homes with modest equity gains, but prevents them from deriving windfall profits from the sale at unrestricted market prices. Given the fluctuations in our real estate market, and as is customary for private second lenders, in the unlikely event of a down trend in housing prices, both the borrower's equity as well as the Agency subsidy would be at risk of loss.

Financing structure	Increase in AMI from date unit initially purchased	Initial purchase and resale prices	First mortgage	Buyer's down payment	Base Price	Agency transferrable shared appreciation loan balance
Purchase: 80% mortgage 15% from RDA 5% from buyers	n/a	\$250,000	\$200,000	\$12,500	\$250,000	\$37,500
First Resale: 80% mortgage 15% from RDA 5% from buyers (Year 5)	30%	\$325,000	\$260,000	\$16,250	same	\$48,750
Second Resale: 80% mortgage 15% from RDA 5% from buyers (Year 10)	60%	\$400,000	\$320,000	\$20,000	same	\$60,000