Council Meeting Date: **November 6, 2017** **Agenda Item:** 9(a)

CITY COUNCIL AGENDA ITEM

CITY OF SHORELINE, WASHINGTON

AGENDA TITLE:	Continuation of Feasibility Study for Transfer of Development Rights and the Landscape Conservation and Local Infrastructure Program in Shoreline
DEPARTMENT:	Planning & Community Development
PRESENTED BY:	Steven Szafran, AICP, Senior Planner Sara Lane, Administrative Services Director
ACTION:	____ Ordinance ____ Resolution ____ Motion _X__ Discussion ____ Public Hearing

PROBLEM/ISSUE STATEMENT:

The Landscape Conservation and Local Infrastructure Program (LCLIP) was passed into State Law in 2011. LCLIP creates incentives for both land conservation in the county and infrastructure improvements in the city. The purpose of the program is to encourage the Transfer of Development Rights (TDR) with a public infrastructure financing tool called tax increment financing (TIF). The City received a grant to study the feasibility of applying LCLIP in the 145th and 185th light rail station subareas, Town Center, and the Community Renewal Area (Aurora Square).

An initial discussion of the LCLIP with Council was held on December 8, 2014. Subsequently, on July 20, 2015, City planning staff, King County staff, ECONorthwest, and Forterra presented the findings of a Shoreline LCLIP Final Report (2015 Report; Attachment A) to the City Council. Staff then conducted further research of the LCLIP program to determine its viability and benefit to Shoreline. Tonight, staff is presenting their findings to Council and seeking direction on next steps.

RECOURCE/FINANCIAL IMPACT:

If the Council chooses to pursue LCLIP for Shoreline, there may be a range of financial implications. The 2015 Report is in need of update, which would cost approximately $20,000 to $30,000.

The 2015 Report finds that the City stands to gain $4.4 million for infrastructure improvements over a period of 25 years if half of the City's growth targets occur and up to $7.3 million if those targets are exceeded from revenue generated by new development. Since 2015, Council has expanded the Property Tax Exemption (PTE) program, also commonly referred to as a Multifamily Tax Exemption (MFTE) program, to the light rail station subareas to further its goal of increasing the availability of affordable housing. A project could be granted a PTE/MFTE that prevents a portion or all of the value of new construction from coming on the property tax rolls for 12 years. The LIPA calculation (described in the response to question 4 in Attachment B) does not capture the value of that new construction until the MFTE expires. Because these changes were made after the report was issued, the report estimates are based on an 8 year MFTE recommended by the consultant. Thus the revenue estimates are overstated if Council wanted to continue with the 12 year MFTE.

In addition, the City must guarantee resources totaling up to $4.6 million to participate in the program, which could potentially leave the City exposed to a $0.2 million loss in the event only half of the City's growth targets occur.

RECOMMENDATION

After evaluation of the program and discussion with other cities, staff does not recommend the implementation of LCLIP at the City of Shoreline. Based on the lack of participation of other jurisdictions, the program's certain obligated costs and the uncertain tax revenue gains for the creation of open space outside of Shoreline, staff believes the complexity and risk associated with LCLIP do not offer enough advantage to the City at this time.

Approved By: City Manager ***DT*** City Attorney ***MK***

BACKGROUND

The Landscape Conservation and Local Infrastructure Program (LCLIP) was passed into State Law in 2011. LCLIP creates incentives for both land conservation in the county and infrastructure improvements in the city. The purpose of the program is to encourage the Transfer of Development Rights (TDR) with a public infrastructure financing tool called tax increment financing (TIF). This program seeks to credit added development potential in exchange for preservation of natural and rural lands in the county, while providing greater assessed tax revenues for the City to pay for improvements such as plazas, parks, sidewalks, bike lanes, etc. to encourage vibrant, livable cities.

An initial discussion of the LCLIP was held on December 8, 2014. The staff report for this discussion can be found at the following link: http://cosweb.ci.shoreline.wa.us/uploads/attachments/cck/council/staffreports/2014/staffreport120814-9a.pdf.

The City began looking at the LCLIP program as a way to include TDRs into the light rail station subareas. In exchange for accepting development rights, the City will have access to financing for revitalizing designated districts. The program would also allow the City to bond against the future tax revenue generated by the development projects to make infrastructure improvements in the conservation districts.

On July 20, 2015, City planning staff, King County staff, ECONorthwest, and Forterra presented the findings of a Shoreline LCLIP Final Report (Attachment A) to the City Council. The staff report for this meeting can be found at the following link: http://cosweb.ci.shoreline.wa.us/uploads/attachments/cck/council/staffreports/2015/staffreport072015-8a.pdf

DISCUSSION

LCLIP Program Overview

As is noted in the Shoreline LCLIP Final Report, LCLIP is a program that offers the use of tax increment financing to a city in return for: 1) the creation of a Transfer of Development Right (TDR) program; and, 2) the acceptance of a specified amount in regional development rights. TDR programs allow additional building area beyond the base zoning in a defined urban area in exchange for the purchase of the right to develop farm and forest lands in a rural area, thus preventing development of those lands.

In exchange for the placement of transferred development rights in LCLIP districts, King County agrees to contribute a portion of its regular property tax generated by the value of new construction within the 25 year period to Shoreline to fund local infrastructure projects cited within the LCLIP district. This is not a new tax to residents or businesses. The remaining portion of the property tax still accrues to Shoreline and King County. Existing and incremental revenues flowing from sales, business and occupation (in implemented), and utility taxes still accrue to the city as if the LCLIP had not been enacted, as well as other capital restricted revenues.

Sponsoring City Ratio

The LCLIP legislation established the total number of transferable development rights that a city is assigned. Shoreline's allocated share from the Puget Sound Regional Council (PSRC) is 231 TDR credits. In adopting an LCLIP program, the city may decide to accept its entire allocated share or a portion of it. This accepted amount is known as the city's specified portion. The "Sponsoring City Ratio" reflects the specified proportion of development rights a city has chosen to accept of the city's allocated share. The resulting ratio (anywhere from 0 to 1) acts to pro-rate the amount of new construction value that can accumulate to an LCLIP district. Details of the calculation for the property tax allocation revenue value for the Local Infrastructure Project Area can be found in the response to question 4 in Attachment B.

Accepting the full allocated share (all 231 credits for a ratio of 1) would maximize potential LCLIP revenues while taking something less than the full allocated share would reduce the potential value of the program to Shoreline. A sponsoring city-specified portion must be equal to or greater than twenty percent of the sponsoring city allocated share.

In choosing its ratio, Shoreline would select an amount of credits it might expect it could place over a 20-year period to meet the threshold requirements and extend the program (and revenues) the full 25 years. Even though the City is allocated 231 credits, Shoreline may accept something less. The minimum number of credits that the City can accept is 46 (20% of 231). This is a similar number accepted by the City of Seattle which has chosen to accept 23% of their 3,440 credits. However it is important to note that both the potential revenue generated by LCLIP and the risk to the City for purchasing credits is reduced proportionately to the percentage of credits that are purchased.

Local Improvement Project Area

A Local Improvement Project Area (LIPA), or LCLIP district, is the designated area in which:

- TDR credits will be placed and measured for performance monitoring.
- Infrastructure projects will be specified and funding will be used.
- The calculation of the new construction as the tax basis for LCLIP revenues will be based.

A city may have multiple and non-contiguous LIPA(s) as long as the area(s) meet the legislation requirement of containing less than 25% of the city's assessed value. Shoreline has potentially identified four areas for use with LCLIP. The areas include the Town Center zone, Aurora Square, and the Station Subareas at 145th Street and 185th Street.

Council should be aware that the same areas identified for LIPA are also the same areas designated for the City's 12 Year PTE.

Transfer of Development Rights (TDR) Options
There are several different methods Shoreline could pursue to place development right credits. The viability of each option varies depending on the geographic areas that the City is considering. LCLIP is a relatively new program, and as a result, the legality of some TDR options is not well established.

Incentive Zoning
One commonly used TDR mechanism is incentive zoning. Incentive zoning allows developers to vary from base zoning requirements by providing some public benefit, in this case the purchase of development right credits. The incentive can either add value to a project by allowing additional height or density, or by reducing project costs through relaxed parking requirements or by providing access to a multifamily tax exemption (MFTE) program, for example.

The City has already adopted these incentives through the Shoreline Development Code in the Town Center, mixed-use residential, and commercial zones. The city allows no density maximums, up to 70-foot high buildings, reduced parking standards, reduced setbacks, and a 12-year PTE for affordable housing. The City is limited on offering any meaningful incentives for TDR purchase when all of the proposed incentives already exist. The consultant recommended Council adopt an eight-year MFTE as an incentive to purchase TDR credits. This prevents the value of new construction from coming on the rolls for eight years, during which time the LIPA calculation would not capture the value of that new construction until the MFTE expires. Some possible incentives for TDR purchase are listed below.

Possible Incentives and Strategies to sell the TDR credits:

- The first 231 units that require affordable housing as an alternative may purchase five TDR credits per unit of required affordable housing. The number of TDR credits required for purchase needs to be some amount less than the cost to construct and maintain the affordable unit. For example, if TDR credits cost $20,000 and an affordable unit cost $140,000 (studio, 1 bedroom @ 70% AMI), then perhaps as an incentive five TDR could be traded for 1 unit of affordable housing. Therefore, the City would trade approximately 47 units of affordable housing (47 units would require the purchase of 231 TDR credits at $20,000 each for $4,620,000) for 231 TDR credits. For perspective, a 200 unit apartment building in the MUR-70' zone requires 40 units of affordable housing. Therefore, the City could easily "sell" all of the required TDR credits through one or two projects in the MUR-70' or 45' zone if the incentive is structured properly. While forgoing affordable units may be a concern, saving open space in the King County for all and the additional revenue estimated at $4.4 to $7.3 million over the 25 year period is a significant benefit. Council could then devote the revenue to infrastructure that directly aids the creation of affordable housing.
- The City could "increase" a development standard to create an incentive. The following could serve as potential examples:
    a. Height could be limited to 35 or 45 feet unless TDR credits are purchased at a defined rate.

b. Density could be limited unless TDR credits are purchased (this may be a less desirable option since the City's zones in the Study areas are form based).
c. Parking reduction could be rescinded and then linked to TDR purchases.

- The City could try a height incentive of an extra floor or two above 65' & 70' maximums for a set amount of TDR credits.
- The City could reduce minimum parking standards for developments within certain zones.
- PTE could be tied to purchase of TDR credits. This would require additional study by those with expertise in LCLIP as the estimated annual savings per unit or per 100 units of new construction would need to be determined in order to determine how many TDR credits would buy a PTE.
- Require a specified subset of development in the Study Areas for LCLIP to purchase a specified amount of TDRs. Example - For every 10 units constructed in the Study Area for LCLIP – 1 TDR credit must be purchased; for every 10,000 sq. ft. of commercial space constructed – 1 TDR must be purchased.
- There are other incentives, such as permit fee reductions; front of the line permitting. These aren't worth many TDR credits and have a resource cost and impact to other permit customers. The City Council would need to evaluate whether from a policy perspective the value of preserved rural lands are a fair exchange for tax subsidized permit activity in Shoreline. Another potential incentive could be a reduction of impact fees. Although this may be an incentive to encourage purchase of TDR credits, State law would require that the City pay for any of the reduced/waived impact fees from general revenues. Again the question of whether preservation of rural properties is a fair exchange for commitment of local tax dollars in Shoreline.
- As another option, Council could make TDRs a requirement in certain zones. Council has already required a portion of rental units in the MUR zones be affordable to certain income levels. Council has also required green building in MUR zones.

Developer Agreements
Developer agreements are a voluntary way for a city to establish standards and conditions for development of a site with the property owner. TDR use can be negotiated into a developer agreement. For example, a TDR purchase reduces the amount of infrastructure improvements required by the development, which lowers development costs, and/or awards density or other bonuses that improve project revenue.

Developer Agreements may be a way to trade city requirements for the purchase of TDR's but the mechanism of a Development Agreement for this purpose is untested and demand is low for this type of permit.

City Purchase with General Revenues
Shoreline could use a portion of its general revenue to purchase all or a portion of its allocated TDR commitment identified by LCLIP. It would first have to estimate the total purchase price of its commitment and the potential return in property tax revenues

through LCLIP. Shoreline could resell those credits to developers when other TDR mechanisms take effect, such as incentive zoning or developer agreements.

The cost of one TDR is approximately $20,000 to $30,000. If the City decides to purchase all of the credits (231) the bill would be approximately $7 million on the high end. The City is taking the risk that development occurs and property taxes can be collected on new projects in the LCLIP district. This is especially risky since new development is not guaranteed.

The risk with this option is the City must meet threshold requirements in order to stay in the program. The City is obligated to buy 25% of the credits within five years, 50% of the credits in 10 years, 75% of the credits in 15 years, and 100% of the credits in 20 years. Assuming the City accepts all 231 credits, the City must place or buy 58 credits in the first five years, 116 credits by year 10, 174 credits by year 15, and all 231 credits by year 20. If the development community is unwilling to buy TDR credits, the City must buy the credits or run the risk of dropping out of the program.

Optional Impact Fee In-lieu

Shoreline could establish an optional impact fee that could be paid in-lieu of existing impact fees. The overall objective of this approach is to leverage existing impact fee payment to achieve an overall higher revenue stream from county property taxes. A development project would have the option of paying a proportionate (but lower) fee into a TDR fund in place of an impact fee. The City would then use those funds to purchase development rights. The additional revenues from LCLIP could be used to pay for projects that would have otherwise been paid for with impact fees and/or other funds.

Shoreline currently offers ways to reduce impact fees and permit fees such as providing affordable housing. There will be competing interests if Council now offers a reduction in impact fees for TDR purchase. Council has been worked to find ways to provide affordable housing, especially in the light rail station subareas where affordable housing is required. Council would have to make a choice if TDRs should come before affordable housing.

District or Citywide New Fee

Total cost of city’s full LCLIP credit allocation is spread across all taxed properties in a district or citywide over 20 years. The city then raises that amount over time (either in districts or citywide) through a fee (creating a new revenue source) to pay for credit acquisition. The actual legality of this method is uncertain and this mechanism has not been used before.

A district fee for TDRs is new and untested. This fee is essentially a Local Improvement District (LID) and the City of Shoreline has never implemented one.

Participation Required

A last option is that the purchase of TDR credits is required for new development as part of an area rezone. The actual legality of this method is uncertain and this mechanism has not been used before.

As Council will read further in this report, some cities in the region do have TDR programs. None of the cities with a TDR program have a requirement for purchasing TDRs. The City already requires affordable housing and green building within the light rail station subareas. Another requirement in these areas may detract new development from locating in these areas.

LCLIP - City of Shoreline

On July 20, 2015, Council directed staff to continue to evaluate the feasibility of implementing an LCLIP program with individual Council members raising some specific questions that they wanted answered during the evaluation. Council's questions are addressed in Attachment B.

While the LCLIP program was marketed as a financing tool for local governments, the amount of "new money" that would be generated is relatively small, estimated at $4.4 to $7.3 million over a very long period of over 25 Years. There are several other factors that make this tool less attractive, including unpredictable timing that limits the ability to do strategic pay-as-you-go or debt financing, financial risk to the City, and the need to potentially sacrifice other goals such as affordable housing to provide incentives for developers. Additionally, the City needs to enter into an agreement with King County that defines the number of TDRs the City is willing to accept. The County also requires the City create a separate Capital Improvement Plan to identify the improvements the City wishes to implement with the LCLIP funds. Should the development community not purchase them, the City would be financially obligated at an amount that could exceed the estimated benefit. Finally, the adoption of LCLIP limits the City's local control over use of property tax revenues. Currently property tax, as a general revenue, is available to support City operations. With the adoption of LCLIP up to 75% of the property tax generated by the value of new construction within the LCLIP districts would be dedicated to the LCLIP districts for specific purposes, thereby limiting the Council's discretion on how to use this general revenue option to support increased demand for operating programs (such as recreation programming, police services, etc.).

Jurisdictions With or Considering an LCLIP Program

The City reached out to a number of jurisdictions that have either adopted an LCLIP Program or are considering an LCLIP program. Questions and responses are listed below. We asked each of the cities the following general questions:

1. How many TDR's have been purchased by developers?
2. Did it achieve the City's goals?
3. Has the City had to or do they anticipate needing to purchase any of the TDRs to meet the City's obligation?
4. Has the City received any of the County shared revenue yet?
5. What incentives are the City offering?
6. Generally, what has the City's experience been with the program?

City of Tacoma

1. How many TDR's have been purchased?
   6 credits, with 14 more in 2018.

2. Did it achieve their goals?
   Not yet. Tacoma is allocated 1,500 TDR's.
3. Have you had to (or do you anticipate needing to) purchase any?
   Not yet.
4. Have you received any revenue yet?
   No, Tacoma is not even close to receiving any revenue and is not forecasted to receive any for the next 10 years.
5. What incentives are you offering?
   The City completed a SEPA Planned Action for downtown so SEPA review and traffic studies are not required. The City has increased Floor Area Ratio requirements (FAR) for downtown development.
6. Generally, what has Tacoma's experience has been with the program?
   Tacoma is still slowly coming out of the recession. Downtown development has been slow and selling TDR's have been equally as slow.

City of Seattle – (Seattle has accepted 23% of their allocated 3,440 TDR Credits)

1. How many TDR's have been purchased?
   About 200 credits, although Seattle estimates it will be about 800 in the next three years.
2. Did it achieve their goals?
   The program is working very well and much faster than expected (due to growth in South Lake Union). Seattle is on track to achieve more TDR purchases than expected and to get substantially more revenue for local improvement than expected. With that said, the money is trickling in slowly so the improvements funded from the revenue will be fairly delayed from the development.
3. Have you had to (or do you anticipate needing to) purchase any?
   No.
4. Have you received any revenue yet?
   Seattle received approximately $40,000 last year and are set to receive approximately $500,000 this year. They are estimating revenue to be over a million the next year and eventually getting up to a couple million a year.
5. What incentives are you offering?
   Increased FAR is the only thing that is of value enough to make a difference. Seattle already had no parking minimums, but even if that were not the case, they are not sure that reducing parking would have been valuable enough to make the program work.
6. Generally, what has Seattle's experience has been with the program?
   The key issues are that:
   - *A lot of modeling is necessary to ensure you have a program that works for the City and the County.*
   - *There is a risk that if you don't reach a certain threshold of development that you will get substantially less revenue than expected.*
   - *You need to balance the value of future, more flexible dollars through LCLIP versus having an incentive program that might get other benefits like open space or green building at the time of construction.*

City of Bothell
The City of Bothell commissioned a feasibility study that is now a few years old. King County and Forterra presented the LCLIP program to the City of Bothell on September 19th. This presentation was similar to the presentation Shoreline received in 2015. The Bothell City Council recommended continuing the discussion and discussing the program in the future.

City of Bellevue
The City of Bellevue is in discussion phase with Bellevue staff.

City of Mountlake Terrace
The City of Mountlake Terrace is not pursuing implementation on account of competing priorities.

City of Tukwila
King County is currently in conversations with the City of Tukwila. The City Council has indicated that they want to pursue LCLIP, however some questions on mechanics remain open. Particularly around how to structure the bonus and use MFTE.

<u>Jurisdictions with a TDR Program (No LCLIP)</u>
Staff has contacted a number of cities in the region to ask about already implemented TDR programs.

City of Redmond
1. Are TDR's mandatory in any of your zones?
   TDRs are not mandatory in any zone, but are one of only two ways to get height bonuses.
2. How many TDR's have been purchased?
   958 TDRs have been transferred but 622 are outstanding (have not been used).
3. Have you had to (or do you anticipate needing to) purchase any credits?
   The City recently recommended to the new Planning Director that we establish a bank to purchase some of the outstanding credits, but that's unbudgeted and not an immediate priority for the department.
4. What incentives are you offering?
   An additional 8,712 square feet of gross floor area (1/5th of an acre); an increase in the maximum impervious surface area by 8,712 square feet; an increase in the height of a building across 1/5th of an acre (8,712sf); or reducing five parking stalls.
5. Does the City of Redmond offer Property Tax Exemption for multifamily (8-yr PTE) or affordable housing (12-yr PTE)?
   Redmond just passed the Multifamily Tax Exemption through council last month and are implementing it right now. They offer the 8- and 12-year exemptions.

City of Issaquah
1. Are TDR's mandatory in any of your zones?
   TDRs are not mandatory in any zone.
2. How many TDR's have been purchased?
   350-400. The City facilitated a big TDR to preserve a large property (Park Pointe) on Tiger Mountain. That work was 350+ units moved from one part of the City to

another. Issaquah also executed a development agreement where 40% of the total entitlement (500 units) had to be acquired thru TDRs. They haven't actually purchased those units as yet, but their development agreement has another 20 years left.

3. Have you had to (or do you anticipate needing to) purchase any credits?
   No.
4. What incentives are you offering?
   Incorporation of TDRs can allow for increased height and increased floor-area ratios.
5. Does the City of Issaquah offer Property Tax Exemption for multifamily (8-yr PTE) or affordable housing (12-yr PTE)?
   Council is discussing it now; possibly "yes" by December.

Pros and Cons for Implementing a TDR Program

Staff has identified the following Pros and Cons for Council's consideration as a staff recommendation was developed on whether to move forward with LCLIP.

Pros	Cons
Financial Sustainability	
Potential for development in the light rail station subareas is greater than that assumed in the 10 Year Financial Sustainability Model, therefore there is a limited impact on the revenue side of the 10-Year Financial Sustainability Model as staff cannot forecast the revenue potential for new construction in these areas resulting from rezoning over the next twenty years.	Restricting 75% of the value of the property tax resulting from new construction occurring within the LCLIP district(s) for infrastructure will reduce the amount of funding available to support the increased level of operating services to accommodate the population growth associated with these new units.
Farmland Preservation	
Preserves farm and forest land in rural King County.	The program would obligate the City to guarantee a certain number of TDR credits. If a developer didn't purchase the credits then the City would be obligated to purchase them. The City's maximum exposure appears to be $4.6 million for $4.4 million in benefits based on TDR credits that cost approximately $20,000-$30,000 per credit. The cost of credits vary depending on the location in the County the development credit is coming from.
Potential Revenue/Risk/Cost	
Could generate between $4.4 and $7.3 million in revenue over 25 years. This is $8.5M to $13.9M in nominal value.	Development (or the City if development does not occur) must purchase 25% of the credits within five years, 50% of the credits in 10 years, 75% of the credits in 15 years, and 100% of the credits in 20 years. Assuming the City accepts all 231 credits, the City must place or buy 58 credits in the first five years, 116 credits by year 10, 174 credits by year 15, and all 231 credits by year 20. If the development

	community is unwilling to buy TDR credits, the City must buy the credits or run the risk of dropping out of the program.
	The City's portion (75%) of the property tax received from new construction is collected for LCLIP and taken out of the General Fund the year the Study Area LCLIP district is established.
	Program timing is very tricky. If the City were to start the program before development begins the City is at a higher risk for having to purchase credits and lose the years to collect the revenue. However, if the City were to start it too late, the City would risk missing out on developers willing to purchase credits. It is further complicated by the timing of the MFTE.
	The program is complex, and will require a: • Negotiated interlocal agreement with King County that must first approve a Shoreline program through their legislative process; • Development of a new plan for projects in the LIPA area, developed in consultation with WSDOT, for the use of the LCLIP revenues; and • Staff oversight will be required to comply with reporting requirements monitoring sale/purchase of TDR credits and to ensure that County property tax distributions impacted by the MFTE are accurate.
	In the best case example, with all TDR rights being sold early, the City would receive an estimated net $176,000 per year of King County property tax levy over 25 years to construct improvements in the LCLIP district. The amount could be much smaller, depending on timing of development, and stretched out for much longer making this a challenging source for debt financing. In short, the amount of money collected does not buy much in terms of infrastructure improvements.
	Forterra is recommending that the City update the feasibility study from 2015 at a cost to the City of an estimated $30,000.
	The program is not well tested. Only Seattle and Tacoma have negotiated agreements for LCLIP.
	The City's zoning regulations do not lend itself to offering incentives such as additional height or additional density for TDR purchase, leaving the options for incentives limited.
	New construction projects in the LCLIP district(s) receiving the PTE will not contribute LCLIP revenue to the program during the exemption period reducing the amount of revenue received in the early periods.

SUMMARY

While the LCLIP program was marketed as a financing tool for local governments, the amount of "new money" that would be generated is relatively small, estimated at $4.4 to $7.3 million over a long period of time (25 Years). There are several other factors that make this tool less attractive, including unpredictable timing that limits the ability to do strategic pay-as-you-go or debt financing for infrastructure, financial risk to the City, and the need to potentially sacrifice other goals such as affordable housing to provide incentives for developers.

Additionally, the City needs to enter into an agreement to ensure that a certain number of TDR rights are sold. Should the development community not purchase them, the City would be financially obligated at an amount that could exceed the estimated benefit. Finally, the adoption of LCLIP limits the City's local control over use of property tax revenues. Currently property tax, as a general revenue, is available to support City operations. With the adoption of LCLIP 75% of the property tax generated by new construction within the LCLIP Districts would be dedicated to LCLIP districts for specific purposes limiting the Council's discretion on how to use this general revenue option. Additionally, there is concern that the incentives necessary may have unintended consequences, such as creating competing goals, to existing programs implemented to achieve Council goals.

It is for these reasons that after evaluation of the program and discussion with other cities, staff does not recommend the implementation of LCLIP at the City of Shoreline.

RECOURCE/FINANCIAL IMPACT

If the Council chooses to pursue LCLIP for Shoreline, there may be a range of financial implications. The 2015 Feasibility Report is in need of update, which would cost approximately $20,000 to $30,000.

The 2015 report finds that the City stands to gain $4.4 million for infrastructure improvements over a period of 25 years if half of the City's growth targets occur and up to $7.3 million if those targets are exceeded from revenue generated by new development. Since 2015, Council has expanded the Property Tax Exemption (PTE) program, also commonly referred to as a Multifamily Tax Exemption (MFTE) program, to the light rail station subareas to further its goal of increasing the availability of affordable housing. A project could be granted a PTE/MFTE that prevents a portion or all of the value of new construction from coming on the rolls for 12 years. The LIPA calculation (described in the response to question 3 in Attachment B) does not capture the value of that new construction until the MFTE expires. Conversely, the City must guarantee resources totaling up to $4.6 million dollars to participate in the program, which could potentially leave the City exposed to a $0.2 million loss in the event only half of the City's growth targets occur.

RECOMMENDATION

After evaluation of the program and discussion with other cities, staff does not recommend the implementation of LCLIP at the City of Shoreline. Based on the lack of participation of other jurisdictions, the program's certain obligated costs and the uncertain tax revenue gains for the creation of open space outside of Shoreline, staff believes the complexity and risk associated with LCLIP do not offer enough advantage to the City at this time.

Shoreline LCLIP

Findings and Recommendations

June, 2015

Prepared for:

City of Shoreline

Final Report

ECONorthwest
ECONOMICS • FINANCE • PLANNING

FORTERRA

HEARTLAND

Contact Information

Morgan Shook, Erik Rundell, Matt Hoffman, and Nick Bratton prepared this report. ECONorthwest gratefully acknowledges the substantial assistance provided by staff at Forterra and Heartland.

ECONorthwest specializes in economics, planning, and finance. Established in 1974, ECONorthwest has over three decades of experience helping clients make sound decisions based on rigorous economic, planning and financial analysis.

For more information about ECONorthwest, visit our website at www.econw.com.

For more information about this report, please contact:

Morgan Shook

ECONorthwest
1218 Third Avenue, Suite 1709
Seattle, WA 98101
206.395.9004
shook@econw.com

Executive Summary

Why is the City of Shoreline undertaking this study?

The City is exploring the viability of the Landscape Conservation and Local Infrastructure Program (LCLIP) for the 185th and 145th Street light rail station subareas, Town Center, and Aurora Square, collectively referred to herein as the Study Areas. The City has created a compelling vision for the Study Areas through recent and ongoing planning efforts that promotes higher levels of activity through mixed-use, high-density development. The growth and development envisioned for the Study Areas can support the City in achieving its broader community goals, such as economic development, fiscal sustainability, environmental conservation, and higher quality of life for its current and future residents.

To catalyze and support growth in the Study Areas, the City will need to make substantial investments in infrastructure. While funding for these capital needs will come from a variety of sources, the City will likely need to contemplate pursuing innovative funding tools beyond those already identified to address potential funding gaps. One funding tool the City is exploring the use of is LCLIP, a form of tax increment financing.

What is LCLIP?

LCLIP is a form of tax increment financing enacted in 2011. The program offers cities access to tax increment financing in return for their acceptance of development rights transferred from regional farms and forests. These transfers are typically conducted as private real estate transactions, but can also be conducted by cities.

In exchange for the placement of development rights in LCLIP districts, the jurisdictional county (in this case King County) agrees to contribute a portion of its regular property tax to the sponsoring city for use for a defined period (up to 25 years). Cities may use this revenue to fund infrastructure improvements that support infill growth and redevelopment. The program is only available to select cities in the central Puget Sound counties of King, Pierce, and Snohomish.

What did the study find?

There is strong policy case for LCLIP in Shoreline.

The analysis shows a range of situations in which LCLIP could succeed. In a scenario assuming that half of the City's PSRC 2035 growth target occurs in the Study Area, LCLIP could generate net revenue of $4.4 million (net present value, or $8.5 million in nominal terms) for infrastructure in Shoreline. Should the City exceed that growth, the net revenue would increase to $7.3 million (net present value, or $13.9 million in nominal terms).

The future light rail station areas can play a role in the city meeting its growth targets. Following a recent rezone, the 185th Street station area has the capacity to accommodate a sizable amount of population and employment growth and already includes a mechanism for using the transfer of development rights (TDR). The pending rezone of the 145th Street station area offers similar possibilities, while developer agreements in Aurora Square and multifamily projects in Town Center could drive TDR use and generate revenue. The City has identified a range of infrastructure improvements, many involving improved mobility and access to transit, in which LCLIP can finance investments that will support redevelopment.

LCLIP will likely be a successful proposition as the local market continues to evolve.

Conditions in Shoreline will support use of LCLIP through redevelopment in the Study Areas. This analysis shows that growth, if in line with projections, is sufficient to make LCLIP a success. At minimum the City would receive new revenue for infrastructure that it otherwise could not access and at best that revenue would exceed $13.9 million. Under such a growth scenario, the Study Areas could support approximately 33 multifamily projects and 32 new retail office projects over a 25 year period.

What is the path forward for LCLIP?

Redevelopment of the Study Areas with more intensive mixed-use development represents a departure from historical growth patterns for some of the areas, particularly those around future light rail stations. The station areas are currently low to medium-density residential areas. The new zoning reflects plans for more mixed-use residential growth near the stations. This change in zoning and potential expansion of uses represents a timely opportunity for the City to finance infrastructure investments that will support that redevelopment. Meanwhile, continued redevelopment of Town Center creates another area in the City that could both support the City's use of LCLIP and also benefit from public improvements. Finally, redevelopment of Aurora Square could be a variable, and potentially influential, contributor to the success of LCLIP in Shoreline. There are three approaches the consultant team identified for proceeding with LCLIP, two of which are likely feasible and can generate revenue for the City.

The current analysis shows that while (1) even with moderate growth estimates the City may net $4.4 million (NPV, or $8.5 million nominal) in new revenue, and (2) a simple and desirable market mechanism can drive the use of TDR. Uncertainty remains around the timing and amount of demand for redevelopment in the Study Areas. However, by taking no action in the near term the City may miss the opportunity to capture value from redevelopment until after the process has already started, thereby passing up potential revenue from LCLIP.

Table of Contents

This page intentionally left blank.

1 Project Overview

In 2014 the City of Shoreline applied for and won a grant through the Environmental Protection Agency's National Estuary Program, administered by the Washington State Department of Commerce. This grant funded a study exploring the viability of the Landscape Conservation and Local Infrastructure Program (LCLIP) for the future light rail station areas at 145th and 185th Streets, Town Center, and Aurora Square, collectively referred to herein as the Study Areas. The City has created a compelling vision for the Study Areas through recent planning efforts that promotes higher levels of activity through mixed-use, high-density development. The growth and development envisioned for the Study Areas can support the City in achieving its broader community goals, such as economic development, fiscal sustainability, environmental conservation, and higher quality of life for its current and future residents.

In order to catalyze and support growth in these areas, the City will need to make substantial investments in infrastructure. While funding for these capital needs will come from a variety of sources, the City will likely need to contemplate other innovative funding tools to address potential funding gaps. The City is exploring the use of the LCLIP, a form of tax increment financing (TIF) enacted in 2011 (RCW 39.108). This program allows cities to access incremental county property tax revenues to fund and finance public improvements within designated LCLIP districts of their choosing. In exchange for receiving a portion of county revenues, cities agree to accept a number of regional development rights of their choosing through a transfer of development rights program (TDR). This program creates a new revenue stream for cities to help pay for infrastructure and is designed to be flexible to suit a wide range of city needs and objectives.

This report provides a series of findings and recommendations for a potential LCLIP program for the City of Shoreline based on:

- LCLIP legislation and program features.
- The City's incentive zoning and possible TDR mechanisms.
- Historical development trends, projections on future growth and estimates of TDR use.
- Estimates of LCLIP funding potential.

1.1 Why Use TDR and LCLIP in Shoreline

The Puget Sound Regional Council's (PSRC) Vision 2040 is the region's strategy for accommodating future growth through 2040. The strategy focuses on concentrating population and employment growth in cities that are best suited for growth and can mitigate many of the public costs and impacts of urban sprawl. Individual cities implement the goals of Vision 2040 through their comprehensive plans and zoning regulations in accordance with the Growth Management Act (GMA).[1]

[1] Washington State Department of Commerce. Website accessed July 2015.

The GMA encourages “innovative land use management techniques” such as TDR to help local governments achieve their planning goals.[2] TDR programs are a tool for implementing growth and planning goals that goes beyond traditional zoning by giving landowners other real estate options, by protecting resource lands from development in perpetuity, and by engaging the market to generate private funding for land conservation.

As mandated by VISION 2040 and by the King County Population and Employment Allocations the City of Shoreline has adopted population and employment planning targets as part of its comprehensive plan, and must act to accommodate that growth within the City over the next 20 years. In addition, the comprehensive plan envisions much of this new growth being directed to the future light rail station areas, Town Center, and Aurora Square.

The Study Areas are anticipated to play a central role in accommodating new growth. These areas have the capacity to accommodate a large amount of population and employment; however, each is in need of infrastructure improvements. The City has limited capacity to pay for all the desired projects through the general fund and existing infrastructure funding sources. As an alternative, LCLIP could help support future growth in accordance with the City’s comprehensive plan by generating revenue to fund improvements that are needed to accommodate that growth and realize the City’s vision.

1.2 Key Questions

This report outlines a series of considerations relating to the use of LCLIP to help inform the City’s decisions on program participation. These considerations will also help the City to understand how to optimize use of the tool in a way that best advances its infrastructure, growth, and conservation objectives. The key questions for this analysis cover:

- What is the policy basis for using LCLIP and broader community goals?
- What are the key LCLIP program issues for how the City may construct its LCLIP program?
- What is the structure of the City’s incentive zoning program and how would implementing a TDR program fit within that structure?
- Under current market and development conditions, how might development projects use TDR to access additional building capacity?
- What range of LCLIP revenues might be possible?
- Based on the cumulative understanding of the questions above, how might the city think about moving forward with an LCLIP program?

[2] RCW 36.70A.090

1.3 Report Organization

The report is organized into six subsequent sections that provide an analysis of the feasibility of LCLIP in the study area and recommendations for moving forward with a Landscape Conservation and Local Infrastructure Program. The main sections of the report are:

- **LCLIP Program Review:** This section reviews the LCLIP legislation and identifies a framework for thinking about incentive zoning, TDR, and LCLIP program choices.
- **Incentive Zoning and TDR Policy Review:** This section reviews mechanisms for TDR within the Study Area and individual zones.
- **Incentive Zoning and TDR Assessment:** This section summarizes the capacity for development and provides an assessment of the feasibility of TDR under current development economics and offers some insight on its potential use.
- **LCLIP Revenue Assessment:** This section reviews development trends in the study area, projects development over the next 20 years. This section then assesses the revenue potential of an LCLIP program under a different growth and TDR absorption scenarios.
- **Program Findings and Recommendations:** This section summarizes the key findings from previous sections and provides recommendations for establishing a LCLIP program based on those findings.
- **Implementation Road Map:** Lastly, this section outlines the steps necessary should the City decide to establish a TDR and Landscape Conservation and Local Infrastructure Program.

2 LCLIP Program Review

2.1 Program Overview

LCLIP is a form of tax increment financing enacted in 2011. The Washington State legislature created the LCLIP program based on its finding that:

The state and its residents benefit from investment in public infrastructure that is associated with urban growth facilitated by the transfer of development from agricultural and forest lands of long-term commercial significance. These activities advance multiple state growth management goals and benefit the state and local economies. It is in the public interest to enable local governments to finance such infrastructure investments and to incentivize development right transfer in the central Puget Sound through this chapter.

The program offers the City a new funding source: a portion of the jurisdictional county's regular property tax in return for 1) mechanisms to place development rights and 2) the acceptance of a specified amount of regional development rights. In exchange for the placement of rural development rights in LCLIP districts, the jurisdictional county (King County for the City) agrees to contribute a portion of its regular property tax revenue to the sponsoring city for use for a defined period. The program is only available to select cities in the central Puget Sound counties of King, Pierce, and Snohomish.

LCLIP targets only a portion of the incremental property taxes generated from new development. This is not a new tax to residents or businesses. The remaining portion of the property tax still accrues to the sponsoring city and to the jurisdictional county. Existing and incremental revenues flowing from sales, business and occupation, and utility taxes still accrue to the City, as well as other capital restricted revenues.

2.2 Use of LCLIP Funds

Under the LCLIP program cities can use LCLIP-generated funds to pay for public improvements in the LCLIP district as follows:

- Street, road, bridge, and rail construction and maintenance;
- Water and sewer system construction and improvements;
- Sidewalks, streetlights, landscaping, and streetscaping;
- Parking, terminal, and dock facilities;
- Park and ride facilities of a transit authority and other facilities that support transit-oriented development;
- Park facilities, recreational areas, bicycle paths, and environmental remediation;
- Storm water and drainage management systems;
- Electric, gas, fiber, and other utility infrastructures;

- Expenditures for facilities and improvements that support affordable housing as defined by WA law;
- Providing maintenance and security for common or public areas; and
- Historic preservation activities authorized under WA law.

LCLIP is different from previous versions of TIF in Washington in that it provides more flexibility on how the funds can be used. Specifically, LCLIP enables funding for more than just capital improvements and can support some operational activities related to the maintenance and security of public areas.

2.3 Determinants of LCLIP Revenues

LCLIP District Revenue Calculation

The tax basis of LCLIP originates from new construction so it excludes existing buildings and revaluation. LCLIP revenues are derived from the allocation of a portion of the City's and County's regular property tax (e.g. current expense levy) to the LCLIP district. Once a district has been created by a city, 75% of the assessed value of new construction – multiplied by a city's sponsoring ratio (explained below) – is allocated to the LCLIP district and used as the tax basis to distribute revenues from the regular property tax using the current year's regular property tax rate.

For example, suppose a newly constructed building generates $1,000 in regular property tax revenues on a property tax rate of $1.00. If this same building is valued at $1,000,000 for the purposes of new construction, then 75% (multiplied by the Sponsoring City Ratio, explained below) of the new construction would place $750,000 in the LCLIP assessed value base and lead to the distribution of $750 of the $1,000 paid in regular property tax to the LCLIP area. The remaining $250 would still go to the jurisdiction's general fund. As noted, the Sponsoring City Ratio acts to pro-rate how much of the 75% of new construction is added to the LCLIP district assessed value base. The example above assumes a ratio of 1.0. Alternatively, a ratio 0.50 would reduce that $750 revenue apportionment to $375.

The calculation of LCLIP district assessed value basis starts at the time that the district(s) is created. The dedication of city and county property tax revenues to the district commence the second year after the district is established. The program can run for a maximum of 25 years on the condition that cities meet performance milestones (explained below).

LCLIP Sponsoring City Ratio

In adopting an LCLIP program, the city must select a specific number of TDR credits to accept based on a regional allocation set by PSRC. These allocations are generally proportional to a city's growth targets; Seattle's allocation is 3,440 credits while Everett's is 1,491 and Tacoma's is 1,843. Shoreline's allocation from PSRC is 231 TDR credits. The "Sponsoring City Ratio" reflects the proportion of development rights a city has chosen to accept (the specific number above) relative to the city's allocated share, as determined by PSRC. The resulting ratio of "specified portion" to "allocated share" (anywhere from zero to one) acts to pro-rate the amount of new construction value that can accumulate to a LCLIP district. A city must set its sponsoring city specified portion that is equal to or greater than 20% of its allocation. For Shoreline, that amount is 46 development rights or higher.

Accepting the full allocated share would maximize potential LCLIP revenues while taking something less than the full allocated share reduces the potential value of the program to a city. For example, Shoreline's allocation is 231 rights; supposing it chooses to accept 58 of them (specified portion), its resulting sponsoring city ratio is 0.25 (58 divided by 231). The City would receive 25% of the county's portion of property tax revenue over the course of the program. If the City accepted 231 credits it would receive 100% of the county's portion.

In choosing its ratio, the city is trying to select an amount of credits it expects to be able to place over a 20-year period to meet the threshold requirements (discussed below) and extend the program (and revenues) to the full 25 years. In doing so, the city is balancing the feasibility/likelihood of TDR being used by development against the amount of revenue LCLIP can generate. Ideally the private market for growth will place all the credits, but as the analysis shows, in a scenario where the private market does not achieve full TDR placement there will be a decision for the city to purchase credits to continue the revenue stream or not to purchase credits and discontinue the program.

LCLIP Performance: Credit Placement Thresholds

While the LCLIP program can run for a maximum of 25 years, the legislation requires participating cities to demonstrate performance on the use of credits within their Local Improvement Project Area (LIPA). Cities using the LCLIP tool must meet a series of performance thresholds pegged to their specified portion and are given a choice in regards to permitting or acquisition of development rights if they want to start and extend the program revenues. These thresholds are as follows:

- Threshold #1: Placement of 25% of the specified portion of TDR credits is required to start the revenue stream. This is not a time-based milestone, but rather a performance-based milestone.
- Threshold #2: Placement of 50% of the specified portion of TDR credits is required by year 10 to extend it by 5 years.
- Threshold #3: Placement of 75% of the specified portion of TDR credits is required by year 15 to extend it by five years.
- Threshold #4: Placement of 100% of the specified portion of TDR credits is required by year 20 to extend it by five years to its conclusion.

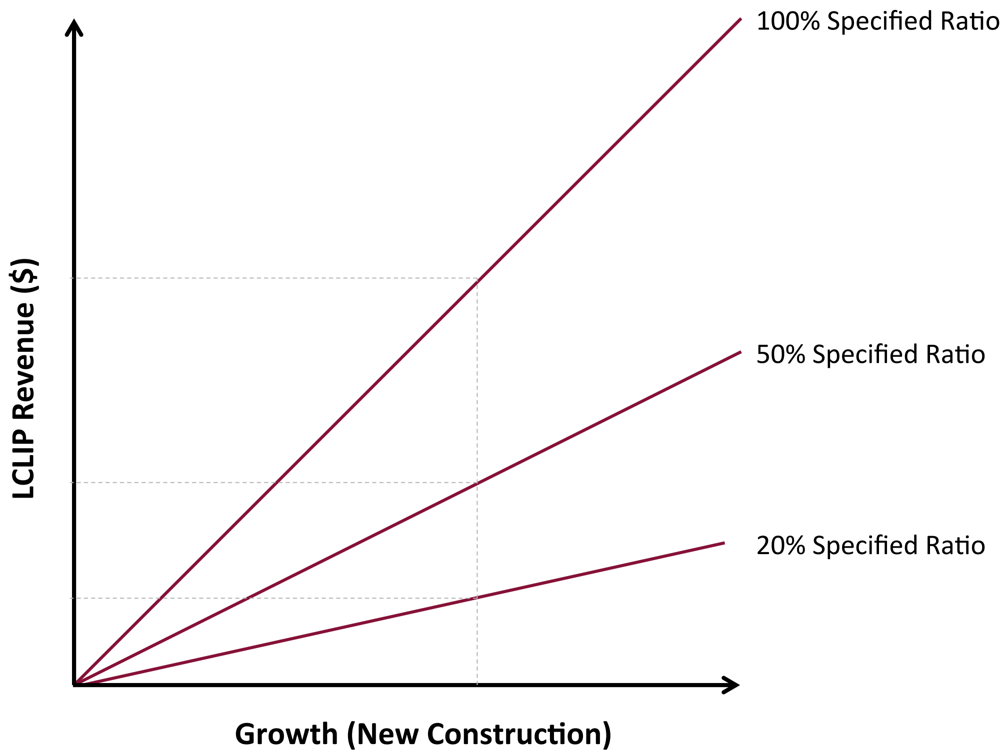
In previous examples of LCLIP implementation, there has been some difference in interpretation from program partners as to what is required to start an LCLIP program. Briefly, the difference in interpretation is whether the placement of 25% of the specified portion is required to start the program or whether the creation of the LCLIP program through ordinance is the trigger. **Should Shoreline adopt LCLIP, this question of timing will be resolved through an interlocal agreement with King County**.

Program revenue is a function of three central factors:

- Specified portion (City TDR credit commitment). Higher commitment = higher revenue
- New construction activity. More construction = higher revenue
- Market participation vs. City credit acquisition. More market activity = more revenue

Exhibit 1 below illustrates the relationships between city TDR commitment, growth, and revenue.

Exhibit 1. Conceptual LCLIP Revenue Scenarios



Source: Forterra, 2015

LIPA(s) District Formation

A LIPA or LCLIP district is the designated area in which:

- TDR credits will be placed by market transfers and measured for performance monitoring.
- Infrastructure projects will be constructed and funding will be used.
- The calculation of the new construction as the tax basis for LCLIP revenues will be based.

A city may have multiple and non-contiguous LIPA(s) as long as the area(s) meet the requirement of containing less than 25% of the city's assessed value. While a city may create multiple LIPA(s), LCLIP works on a cumulative citywide basis and not an independent district basis – meaning the same program parameters apply to all LIPA(s) regardless of start date and configuration. Therefore if a city is considering multiple LIPAs, it is advantageous to establish them all at the program launch rather than adding them incrementally over time, which would result in foregone revenue.

2.4 Program Framework for LCLIP

A strong LCLIP program for the City of Shoreline must position the City to maximize LCLIP revenues through structuring the following program parameters:

- **LIPA geography.** The City will want to create a LIPA(s) that meets the nexus requirements stated above. However, creating a district(s) that contain areas where development is expected will help create a large new construction tax base used as the basis of the revenue calculation. The larger the tax base, the more funding leverage the City will have.
- **TDR provisions.** The number of TDR credits used is a function of several factors:
  - <u>The size and structure of the incentive component.</u> The city must determine how much demand there may be for building projects that will utilize TDR. The placement of TDR within the structure of the incentive mechanism factors in how it may be accessed by developers. For example, TDR may be among a menu of options that developers can choose from, it may be tiered with other options requiring developers to sequence options that may place TDR first or last in that sequence, or it could be the means by which developers access cost savings.
  - <u>The nature of the incentive associated with TDR.</u> Typical TDR incentives offer additional FAR or height; however, TDR can be connected with any variety of opportunities associated with development ("conversion commodities"). Other examples include connecting TDR with reduced setbacks, structured parking requirements, or impervious surface limitations. In the context of Shoreline, the incentive may be a multifamily tax exemption, part of a negotiated development agreement, or incentive zoning.
  - <u>The exchange rate for TDR.</u> The amount of incentive a developer receives per TDR credit used in large part determines the extent to which a TDR consumes the incentive zoning available. The incentive created by the TDR exchange rate must be equal to (or exceed) a developer's willingness- and ability-to-pay, otherwise TDR will not be used.
- **City specified portion and program timing.** In order to optimize the flow of LCLIP revenues, the City has an incentive to meet all four performance thresholds. Doing so means the city must select a specified portion that is targeted at some expected use of incentive zoning and the absorption of TDR credits over the horizon of the program. This element of LCLIP is the most difficult technical aspect that the city must consider. Forecasting future development is challenging, much less determining the rate at which that development will access incentives that use TDR.

3 Incentive Zoning and TDR Policy Review

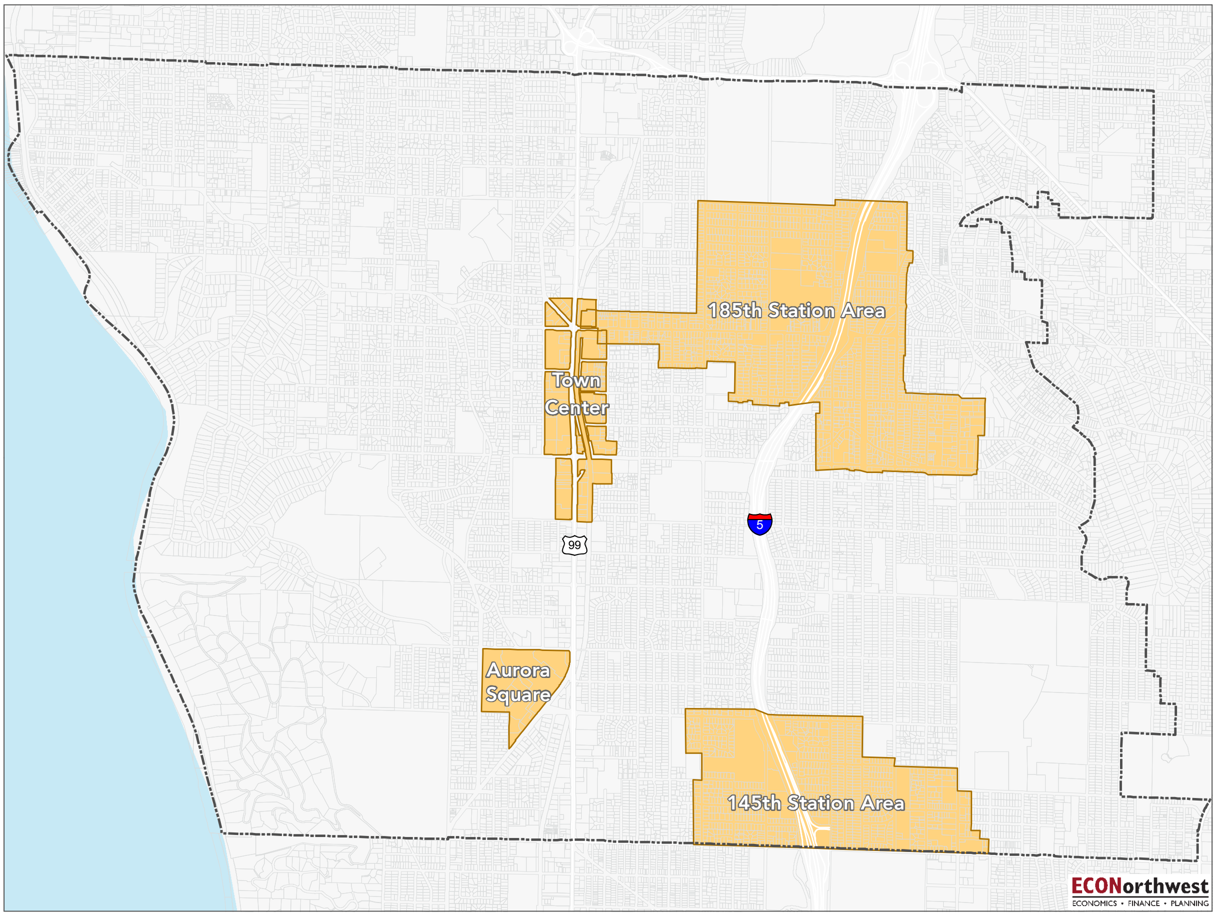
Overall, Shoreline's existing policies support the use of TDR and LCLIP. Shoreline currently offers incentives to advance affordable housing and density goals, although not in the form of incentive zoning. Shoreline does not currently have a stand-alone TDR program, however the 185th Street subarea plan includes a TDR provision.

Shoreline's comprehensive plan language establishes a policy foundation for the use of LCLIP and TDR to encourage quality development, revitalize neighborhoods, and provide infrastructure that supports growth. Shoreline should look to the comprehensive plan goals and policies to determine areas that LCLIP funding should be directed towards. Shoreline may consider using LCLIP as a source of funding to meet the goals of catalyzing a master-planned, sustainable lifestyle destination in Aurora Square. Additionally, light rail station expansion areas would benefit from infrastructure investments as the city plans to work with stakeholders to identify and funds additional improvements that can be efficiently constructed in conjunction with light rail and other transit facilities.

3.1 Study Area Context

The City has four different areas within Shoreline it is evaluating for LCLIP feasibility. The areas include the Town Center zone, Aurora Square, and the future Link light rail station areas at 145th Street and 185th Street.

Exhibit 2. Overview of Study Area



Source: City of Shoreline, King County

3.2 Existing Incentives

Real estate economics show that the value of building a home on a single-family lot in a rural area is considerably higher than the marginal value of an additional unit constructed in an urban multifamily receiving area project. To address these different values and incentivize the use of TDR the benefit to developers in a project must exceed the cost of buying credits. One way to achieve this goal is to offer developers more units in a project than are being removed from rural areas. For example, in the King County TDR program a developer gains the ability to construct two bonus units for every one TDR credit purchased. A similar approach will be useful in Shoreline to create sufficient incentive.

The City currently only encourages the utilization of TDR credits in the 185th Station Area where the first 300 units may access the eight-year MFTE program and do not have to provided the required affordable housing in exchange for TDR credits. The code dictates that projects may access this incentive if one TDR credit is secured for every four units. While this is currently the only requirement in place to use TDR credits, the LCLIP program is flexible and allows for multiple approaches to achieve market-based credit placement. Options the City might consider include the expansion of incentive zoning in the Town Center, Mixed Business zone, or potentially the 145th Station Area; an expansion of the current code in the 185th Station where private placement via a multi-family tax exemption is an incentive; development agreements; public acquisition of credits; or a combination of approaches to create a portfolio of mechanisms to place TDR credits and meet LCLIP performance milestones. The following summarizes each approach.

Incentive Zoning

Incentive zoning or the exchange of additional development capacity in return for a public benefit is a common approach to utilizing TDR credits. This can be in the form of additional height, additional units, lower parking ratios, or a reduced lot coverage ratio to name a few.

Private Placement

Another alternative is private placement through other incentives such as requiring the use of TDR credits to access the MFTE program. The concept MFTE is simple: developers receive an eight-year exemption from property taxes for constructing multifamily residential projects that provide a public benefit. Later sections detail this approach, along with costs and revenues associated with the mechanism. This approach would be considerably simpler from a policy and regulatory standpoint to implement than incentive zoning that includes TDR, and could potentially reduce uncertainty in implementation of LCLIP by providing a more streamlined and valuable bonus to developers.

Development Agreements

Another avenue by which the City can generate demand for TDR credit placement from private development is with development agreements. This approach is more opportunistic than MFTE or incentive zoning, and is more variable in its ability to absorb credits. When a developer proposes a large project to the City and requests special dispensations to facilitate its construction the City has an opportunity to negotiate the acquisition of TDR credits by the developer into the agreement. There is no formula or guideline for this, and since the pipeline of projects that could potentially place credits is uncertain the viability of this approach is difficult to predict with certainty. A single large project, however, could result in the placement of a substantial portion of the City's TDR commitment.

Public Acquisition

While not likely the first choice for the City as a means to meet performance milestones in LCLIP the use of public funds to acquire credits needed to continue the program is another option. Any public money that the City expends to buy credits to achieve milestones reduces the net revenue that would accrue to the City. That being said, it is important to keep as a backstop to close any gap left by the private market. The City could negotiate pricing agreements with King County or other flexible terms as part of an interlocal agreement implementing LCLIP. The revenue projections for the City are such that even if public acquisition became necessary the City would still come out ahead financially – possibly far ahead – given the prospects for the program.

3.3 Incentive Zoning

Shoreline currently offers a variety of incentives to developers to encourage affordable housing, density, and high quality development. However, Shoreline does not currently have a formal incentive zoning program. Shoreline's zoning in the Study Areas suggests that bonus options other than additional units or floor area would be potential approaches to pursue for TDR utilization. For example, there are no incentives currently offered for additional height. This would potentially make bonus height an incentive for a TDR program in areas where the City deems it appropriate. That said, in the Town Center commercial zones, as well as Mixed Business, multifamily residential buildings are permitted to be built up to 70-feet and 65-feet, respectively. These heights may support up to seven-stories. However, the resulting floor heights are not optimal under situations where the ground floor space is required to be taller than 10-feet (typically 15-feet ground floor height).

At these permitted heights we assume most developers would develop six-story multifamily residential projects often referred to as five-over-one construction types.[3] An additional floor would support five-over-two projects. Changes in building and fire codes are allowing cities to permit these seven-story projects and this extra floor could be a land use code modification that uses TDR credits. While there is an added cost to constructing an extra level this is often offset by the added revenue potential from additional units.

Additional TDR incentives that award parking reductions or impact fee offsets could be considered in light of existing incentives offered to promote other public benefits, particularly around future station areas. The current land use code and proposed language in the 145th Station area provide for typical market based ratios.

One opportunity for TDR use under current market conditions is within the Town Center and potentially the 145th Station Area where buildings are currently permitted to achieving 65 to 70 feet. These zones provide an opportunity to test the impact of an additional story on project economics. Modeling a hypothetical project provides insight into what a developer could afford to pay for bonus density holding other factors constant.

Market, revenue, and cost inputs were derived from an analysis of comparable projects in the surrounding area to arrive at a set of key analysis assumptions (below). These include physical programming such as podium sizing, building efficiency, and average unit sizes as well as market data such as rents, expenses, cap rates and typical developer profit assumptions.

In both cases the project was modeled assuming wood frame construction atop a concrete podium (Type V-A construction). This concrete podium encompasses all ground-floor uses, including a 2,500 square foot retail component, lobby and residential community space, and at-grade, "tucked," or

[3] The five over one construction type is an abbreviation for Type V construction over Type I construction or wood frame over concrete and steel construction. This construction can be in six stories with one level of concrete and five of wood frame or seven stories with two levels of concrete and five levels of wood frame.

"wrapped" parking. Podium height is assumed to be 15 feet, commensurate with market demand for Class-A retail space. Additional required parking is accommodated with surface parking to avoid costly below-grade structured parking. The prototype used for this assessment was the Malmo development. This project has recently been completed and comprises 129 units in a five over one construction type building. This project sits on 1.2 acres.

Space Program Comparison

In this example, an incentive of an additional floor (10' heights) is achieved with design bonuses through the provision of retail and public space. With the above assumptions, the modeled project yields 148 units within a 70-foot tall structure. Including a TDR bonus density through the addition of a story the project yields and additional 24 units - for a total of 171 units. The additional floor is of type one construction with a portion of the level being used for parking and a portion for residential units.

Financial Performance

Based on the current market, a five-over-one or five-over-two development type would be feasible if land values are at or below $34 per square foot. The project economics are similar between the two types because the cost of the additional floor of concrete construction is roughly in balance with the additional units and subsequent revenue potential. Developers may elect to construct an extra floor if the market would support a higher rent. As shown in Exhibit 3, the likelihood of an incentive requiring TDR credits to add an additional floor would not likely result in TDR credit utilization. This is indicated by the similar resulting residual land values between the two scenarios.

Exhibit 3. Bonus Density Pricing

Key Inputs	Base w/ Design	TDR	Type	Key Outputs	Base w/ Design	TDR	Increment
Use	Apartment	Apartment		**Density**			
Regulatory				Stories	6	7	**1**
Zoning	Mid-Rise	Mid-Rise		Height	65	80	**15**
Max Height	65 to 70	80	ft	Floor Area Ratio	4.00	4.90	**1**
Max FAR	NA	NA		**Space Program**			
Space Program				BGSF	134,100	155,225	**21,125**
Unit Size (NRSF)	705	705		Unit Count	148	171	**24**
Parking Ratio	1.00	1.00		Parking Stalls	133	154	**22**
Lot Size	50,000	50,000		Retail SF	5,000	5,000	**0**
Revenue				**Financial Performance**			
Rent	$1.95	$1.95	psf/mo	Proj Value	$29,148,428	$33,796,308	**$4,647,880**
Cap Rate	5.75%	5.75%		Proj Cost	$25,129,828	$29,203,829	**$4,074,001**
Expenses				Margin on Cost	16%	16%	**14%**
PUPY Cost	$5,700	$5,700	per unit/yr	**Value Remain for Land (RLV)**			
RE Taxes	$1,539	$1,539	per unit/yr	Total	$1,686,725	$1,888,774	**$202,049**
Returns				RLV / Unit	$11,434	$11,014	**-$420**
Developer Profit	16%	12%	on cost	RLV / Land SF	$33.73	$37.78	**$4.04**

Source: Heartland

There are other opportunities in the 185th Station Area and potentially in the 145th Station Area for utilizing TDR credits for additional height beyond just a single floor. According to the land use code for the 185th Station Area buildings in the MUR-70 zone buildings may exceed 70-feet (heights tall enough to support five over two construction) through a development agreement. However, the market economics to support multifamily towers in the City are several development cycles away and the likelihood of any towers being built during the LCLIP program is low.

3.4 Private Placement

The only area in Shoreline where TDR is currently allowed is the 185th Street station subarea, and this provision is subject to the City authorizing a TDR program. For the first 300 units of multifamily housing constructed, developers may access an eight-year property tax exemption and forgo the affordable housing requirement by acquiring TDR credits at a rate of one credit for every four units built. This would result in the placement of 75 TDR credits.

The other Study Areas (145th, Town Center, and Aurora Square) could also use an eight-year property tax exemption to place TDR credits. Under RCW 84.36 a city may grant a developer an eight-year exemption on property taxes if a multi-family project provides some public benefit. This mechanism has traditionally been used to incentivize the construction of affordable housing and can also apply to TDR and the LCLIP program, which clearly provides multiple public benefits.

Under this approach, the bonus that the developer would gain is access to operational cost savings through the eight-year tax exemption. In order to access this, the developer would buy TDR credits. The number of credits needed to access the MFTE would be calibrated such that the net savings to the developer is still sufficiently high to justify the credit purchase.

Analysis of developer willingness to pay suggests that a prototypical 120-unit project could place approximately 40 credits. This model results in **an exchange rate of one TDR credits per three units in the project or a fee in lieu of $25 per net square foot** assuming an average unit size of 800 square feet and the average TDR credit costs $20,000 today. By participating in this program the owner of this prototypical project could realize a tax savings of nearly $473,000 in nominal terms over the eight-year exemption for very little effort. This assumes that 65% of the benefit goes toward TDR acquisition and the remainder to the project owner. The City would need to amend its development regulations to define the terms and create the mechanism for developers to access MFTE through purchase of TDR credits. The table in Exhibit 4 summarizes the approach used to estimate TDR utilization.

Exhibit 4. TDR Credits to Access MFTE Program

		Annual Tax Δ	Split	TDR Cost:	$20,000
		1%	65%	Inflation:	2%
	Year	**MFTE Benefit**	**TDR Contribution**	**Project Tax Savings**	**TDR Credits Afforded**
1	2015	$163,200	$106,080	$57,120	5.2
2	2016	$164,832	$107,141	$57,691	5.1
3	2017	$166,480	$108,212	$58,268	5.1
4	2018	$168,145	$109,294	$58,851	5.0
5	2019	$169,827	$110,387	$59,439	5.0
6	2020	$171,525	$111,491	$60,034	5.0
7	2021	$173,240	$112,606	$60,634	4.9
8	2022	$174,972	$113,732	$61,240	4.9
	Total	$1,352,221	$878,944	$473,278	40.2
	NPV	$967,464	$628,852	$338,612	

Total credits over 8 year period for a 120 project	40.2
Exchange Rate 1: TDR credits needed per 3 units	1.0
Exchange Rate 2: Fee in lieu per net square feet	$25

Source: Heartland, 2015

The MFTE program does come with an opportunity cost for the City in the form of tax revenue reallocation during the eight years these units are exempt. The MFTE program would delay the new construction value contributions to the LCLIP program for the City until the eight-year exemption expired. After the exemption expires the value would be added to the City's assessed value used in calculating how much revenue the City is receiving under the program. The delay in adding new construction value will somewhat reduce the amount of LCLIP revenues to the City over the life of the program. The City would also realize slightly less in total property tax revenue due to the delay in the addition of new construction value as well. Further analysis may be warranted to study the fiscal impacts of this program relative to the benefits of added units and LCLIP revenue.

Based on this analysis we assume that the first 300 units in the 185th Station Area will use the MFTE incentive meaning 75 credits out of the 231 (under a full acceptance of credits by the City) would be utilized leaving 156 credits. If the other study areas are offered a similar incentive, but a one credit per three unit rather than one credit per four unit then only 468 more units would need to be delivered to support the LCLIP program. In total this would represent 768 units or between six to eight multifamily projects assuming an average project size of 100 to 120 units.

For Aurora Square, where rules around Community Renewal Areas allow the City greater flexibility in specifying terms for redevelopment and where zoning is not conducive to a traditional TDR incentive structure, a more appropriate mechanism for using TDR would be to include acquisition of credits as part of a negotiated development agreement. In this situation an exchange rate may not apply; rather the City and developer would agree on a total number of credits to buy as part of the terms of the project.

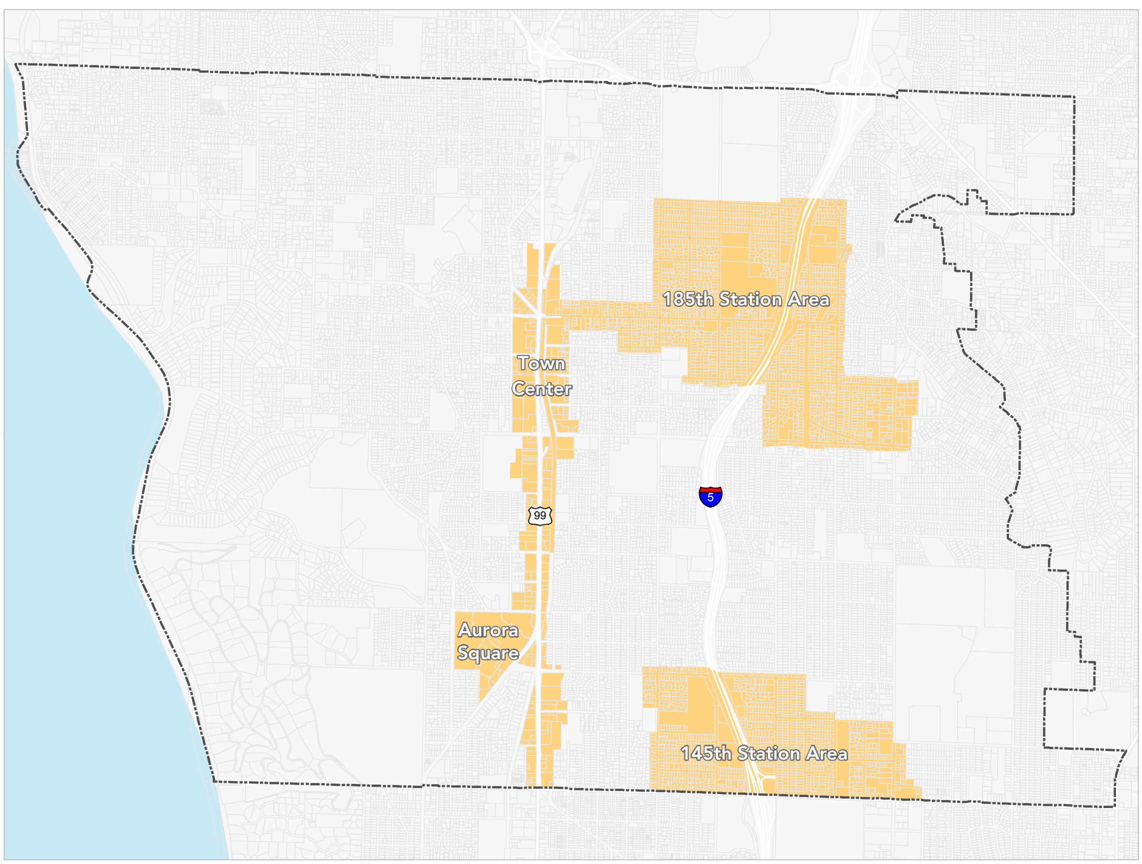
4 LCLIP Revenue Assessment

The LCLIP revenue assessment tests several parameters to better understand the impact of different TDR mechanisms and development growth variables as drivers of potential LCLIP revenues. LCLIP revenues are dependent on a few different inputs, primarily the LIPA area used and the projected amount of growth within that area. The next two sections discuss these in more detail before then assessing the revenue potential under different scenarios.

4.1 LIPA Area

For the revenue analysis, the initial combination of four discrete geographies was examined. Upon reviewing the revenue-generating potential for the Study Areas, the analysis showed that collectively these areas represented only 14% of the City's total assessed value. Two key features of LCLIP are that revenue is a function of growth and cities may capture the incremental revenue from up to 25% of their assessed value. It is to Shoreline's advantage to maximize the assessed value included in the LIPA in order to maximize the program's revenue potential. Subsequent revenue projections were based upon an expanded Study Area that extended north and south along Highway 99 from the Town Center, which is shown in Exhibit 5.

Exhibit 5. Expanded Study Area



Source: City of Shoreline, King County

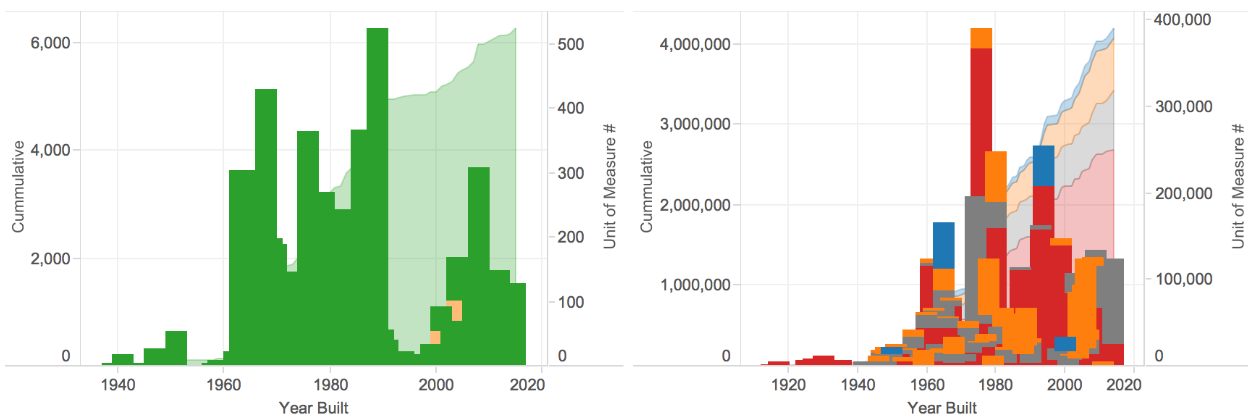
4.2 Development Assessment and Projections

This section provides an assessment of development trends in the study area in order to understand real estate development shifts in the area and make reasonable projections about possible future growth, based on those trends and near-term projects in the pipeline.

Based on the City's buildable land assessment and capacity analysis estimate there is enough land and zoning capacity to support approximately 9.1 million square feet of commercial space and just over 5,000 units. These estimates were calculated prior to the rezone of the 185th Study Area approval and the potential additional development capacity that may result from the rezoning of the 145th Study Area. Based on figures from OTAK, combined these two areas could increase the city's capacity up to 10.1 million commercial square feet and 42,730 multifamily units.

Exhibit 6 below helps put that capacity into perspective. The chart on the left shows historic multifamily development patterns through April 2015 in units delivered city-wide while the chart on the right shows historic commercial development patterns by net square feet delivered[4]. The city has just over 6,000 multifamily units (project with at least four units or more) and the cumulative total of commercial space in the city is just over four million square feet. Based on this assessment there is ample capacity to support new development for decades to come.

Exhibit 6. City Development Patterns



Source: Heartland LLC

The growth scenarios devleoped for LCLIP Revenue Testing were based on the PSRC's growth targets for the City and the three study areas as well as the property comprising Aurora Square and commercially zoned land within 500-feet of Aurora from the southern end of the city to the north just past the Town Center Study Area. The reason for including the latter two areas was to test potentital revenues from a LIPA that approaches the LCLIP programs 25% of the city's current assessed value.

The table in Exhibit 7 summarizes PSRC's household growth estimates between 2010 and 2035 for the City as well as the Study Areas. Also depicted in this table are estimated number of new housing

[4] Parking structures are non-leasable square footage are typically excluded from the King County Assessor's net square footage calculations.

units that may be introduced to support the household growth. These estimates are based on pre-Study Area rezone condition.

Exhibit 7. PSRC Growth Target Summary

	Area	2010 Households	2035 Estimated Housheolds	Estimated Household Growth	Estimated Housing Unit Demand	Estimated Multifamily Unit Demand*
	City of Shoreline	**21,576**	**26,711**	**5,135**	**4,602**	**2,591**
Study Areas	145th Study Area	1,132	1,601	469	419	419
	185th Study Area	1,690	2,141	451	403	403
	Town Center Study Area	395	595	200	179	179
	Aurora Square/Corridor**	4,232	5,657	1,425	1,275	892
	Study Areas Total	***7,449***	***9,994***	***2,545***	***2,276***	***1,893***
	Study Areas % of City	*35%*	*37%*	*50%*	*49%*	*73%*
	City Remainder	14,127	16,717	2,590	2,326	698

Source: PSRC, Heartland LLC

Notes:

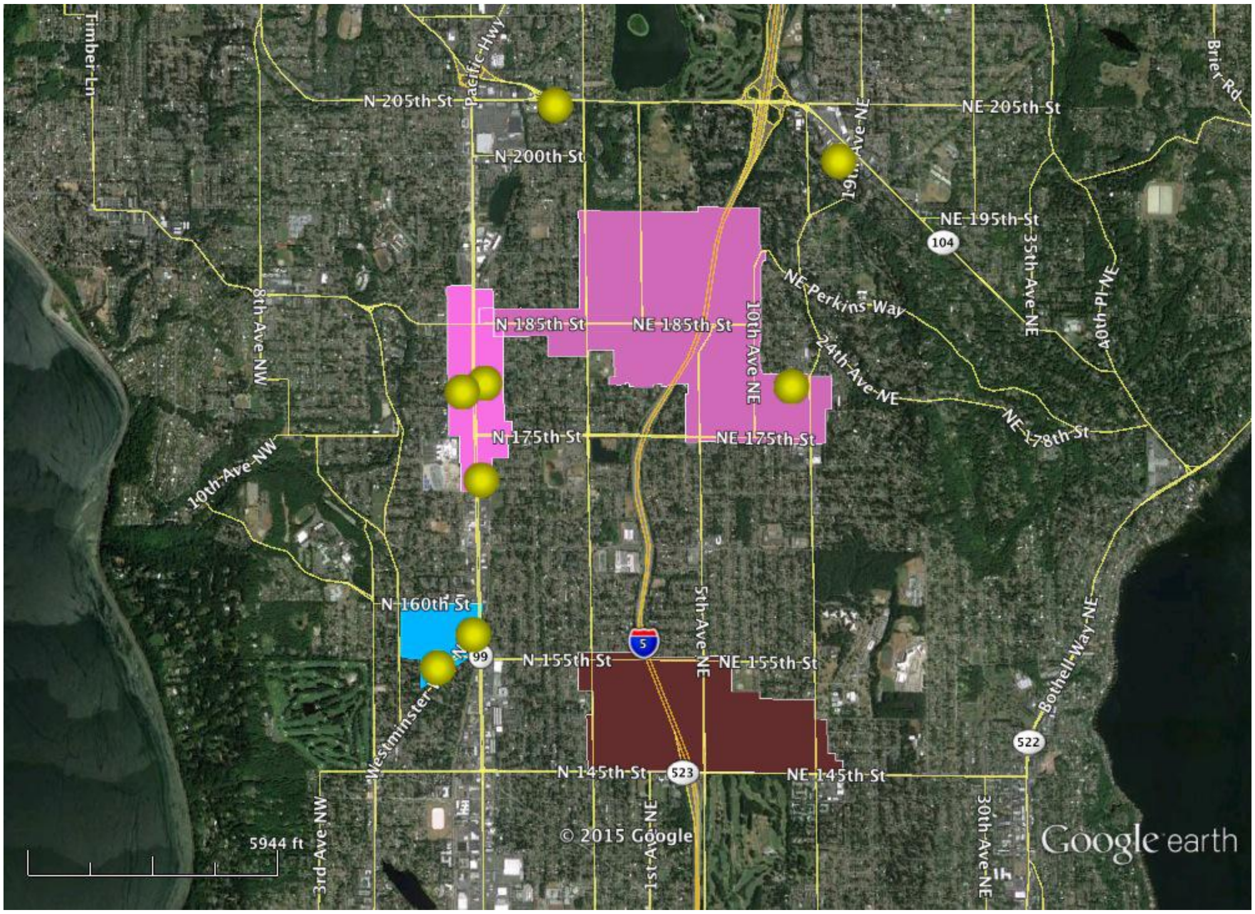
* Esimated multifamily unit demand assumes that 100% of the housing units delivered in the 145th, 185th, and Town Center study areas will be multifamily units while 70% of the units in the Aurora Square/Corridor area will be multifamily and 30% of the city's remaining household growth will be supported in multifmaily developments.

**The City, Town Center, 145th, and 185th Study Areas household estimates were provided by PSRC from its Land Use Targets data. The Aurora Square/Corridor estimates are based on PSRC's TAZ areas that touch the Aurora Square/Corridor area.

The PSRC is revising its growth targets and Shoreline's will likely increase as a result of this effort. This will be due to the additional capacity that the rezone will allow coupled with the City's proximity to job centers and the improved connectivety to those job centers via bus rapid transit imporvments and the planned Sound Transit Link Lynnwood extenion.

The development pipeline in the City illusrates it's growting attractivness to developers. Rental rate trends (driven by low vacancy rates) are supporting new multifamily projects. Exhibit 8 on the following page maps a list of key pipeline projects that will account for growth in the study area in the near-term. In the coming years, over 1,062 new residential units in 8 projects are planned with 215 of the units scheduled for delivery in the next two years. These projects are generally indicative of the type and scale of growth going forward.

Exhibit 8. Pipeline Sites



Source: Heartland

Development Projections

A look at historical delivery of mulifamily units and commerical square footage would suggest the current growth targets are likley attainable. However, with the regions projected growth, the obseved recent development trends, and a strenghtening regional market, Shoreline should be able to easily meet and exeed PSRC's growth target. As a result, two growth scenarios were developed for LCLIP revenue modeling. The following table in Exhibit 9 summarizes the multifamily and commercial projections for all of the Study Areas under the Growth Target Scenario over a 25-year period.

Exhibit 9. Growth Target Development Projection in Square Feet

Area	Commercial	Multifamily Units	Multifamily Projects	Parking Structures	Total Square Feet	Distribution
185th	16,307	544	5	102,261	662,146	11%
145th	15,993	533	4	100,290	649,383	11%
Town Center	765,431	265	2	381,198	1,411,329	24%
Aurora Square	258,988	518	4	203,953	980,917	17%
Aurora Remainder	900,382	744	6	524,109	2,168,442	37%
Total	1,957,101	2,603	22	1,311,810	5,872,218	100%

	Multifamily Units	Projects	Commercial Square Feet
First 10 Years:	810	7	602,078
Remaining 15 Years:	1,793	15	1,355,024

Source: Heartland

The second scenario, illustrated in Exhibit 10, summarizes the High Growth Scenario where the pace is projected to increase a greater rate than the Growth Target Scenario in all of the areas over a 25 year period.

Exhibit 10. High Growth Target Projections in Square Feet

Area	Commercial	Multifamily Units	Multifamily Projects	Parking Structures	Total Square Feet	Distribution
185th	23,296	777	6	146,087	945,923	11%
145th	20,562	685	6	128,944	834,922	10%
Town Center	921,813	319	3	441,280	1,682,163	19%
Aurora Square	517,976	1,036	9	407,906	1,961,835	23%
Aurora Remainder	1,350,573	1,116	9	786,163	3,252,663	37%
Total	2,834,221	3,933	33	1,910,379	8,677,506	100%

	Multifamily Units	Projects	Commercial Square Feet
First 10 Years:	1,238	10	879,804
Remaining 15 Years:	2,695	22	1,954,416

Source: Heartland; PSRC

4.3 LCLIP Revenue Testing – Scenarios

Overview

Using a LCLIP revenue model designed for the City, the analysis tested three different scenarios to assess the number of TDR credits potentially placed and corresponding revenues generated through the LCLIP program. Each scenario assumes different levels of growth to test how sensitive the revenues are to the assumed amount of growth.

Assumptions

The analysis uses a number of common assumptions for all scenarios. The revenue analysis assumes that the primary mechanism used to place TDR credits is the eight-year multi-family tax exemption (MFTE) program. It is likely a large share of new multi-family residential development would use the MFTE program. The program is voluntary, but if structured correctly, the property tax exemption would provide a cost saving to the developer after purchasing development rights, creating a financial gain for purchasing credits. LCLIP revenues in the scenarios below include the delay in property tax revenues due to using the MFTE mechanism.

The analysis assumes that the LCLIP program would start in 2016 and run for 25 years. For a program starting now the net present value is a useful measurement of projected revenue, as it is adjusted for inflation. For a program starting in the future it is helpful to consider the revenue stream over time in nominal terms (not adjusted for inflation). Considering both values provides a more complete picture.

All scenarios assume the price of TDR credits is $20,000 and increase to $36,000 (in 2015 dollars) at year 15. The analysis also assumes all TDR credits are first purchased by the private market, and the City only purchases credits to meet the program placement thresholds to continue the program going if needed. The exchange rate for the program is based on the assumed value of the tax exemption relative to the cost of purchasing TDR credits. For the exchange rate, about three units need to receive the exemption over eight years to justify paying for one $20,000 credit.

The Impact of Development Variables

The following scenarios assessed LCLIP revenue based on assumptions about the timing, scale, and quality of development. Outside of the LCLIP program parameters, the three main development-based determinants of revenue impact are:

- **Scale and mix of development.** The revenue impact is likely to change as developers contemplate differing types and amounts of residential and commercial development.
- **Value of development.** While the baseline assumptions around development value (normalized on a square footage basis) were drawn from reliable data, it is difficult to predict future development value with great certainty.
- **Timing of development.** The timing of construction can either accelerate or delay the delivery of LCLIP revenues. Delay reduces the revenues under the LCLIP time window by pushing out the returns into the future, resulting in reduced years of benefits that are discounted more heavily. The opposite is true in a situation where development happens earlier.

It should be noted that changes to any of these (whether driven by future policy or market dynamics) can have a significant impact on the amount of LCLIP revenue generated. A difficult issue to disentangle from the analysis is the degree to which potential LCLIP-driven infrastructure improvements may facilitate (i.e. lower the overcall cost or feasibility) development by solving critical site and/or access issues or by reducing costs to developers.

Scenario 1: Growth Target Forecast with Limited MFTE Program

This scenario assumes 3.7 million square feet of development occurs within the Study Areas by 2040. This level of growth represents 50 percent of PSRC's 2035 growth target for the City. This scenario assumes the first 300 units constructed in the 185th Station Area are eligible for the eight-year MFTE program and affordable housing waiver.

Under this scenario the City would not be able to meet the first performance threshold at year ten, which requires placement of 116 credits. This scenario assumes half of the projected growth for the 185th Station Area occurred over the first ten years and 80% of the first 300 multi-family units in the 185th Station Area used the MFTE program. As a result, only 54 credits would be placed in the first ten years. The City would need to purchase the additional 62 credits to continue the program at a cost of over $1.35 million in 2015 dollars.

Relying solely on the MFTE program in the 185th Street station area will not create a viable path for LCLIP success without City support or finding other options for placing TDR credits within the other components of the Study Areas.

Scenario 2: Growth Target Forecast with Full MFTE Program

Scenario 2 tests how many credits the MFTE program could utilize if the eight-year multi-family tax exemption (MFTE) program was enacted in the entire Study Area at the start of the program. This scenario also assumes the City would realize the same 3.7 million square feet of new development by 2040 as in Scenario 1, but it uses the lower exchange ratio of one TDR credit for every two units, which means the program could retire more TDR credits for the number of units constructed. It also assumes that 80% of multi-family residential development in these areas would utilize the program. This figure is derived based on utilization rates in the City of Seattle. Lastly, the scenario also assumes that the City accepts 100% of the 231 allocated credits to maximize revenue.

Under these assumptions the LCLIP program would place all 231 credits of the City's TDR credit allocation. In addition, the private market could retire enough credits to meet all of the performance thresholds.

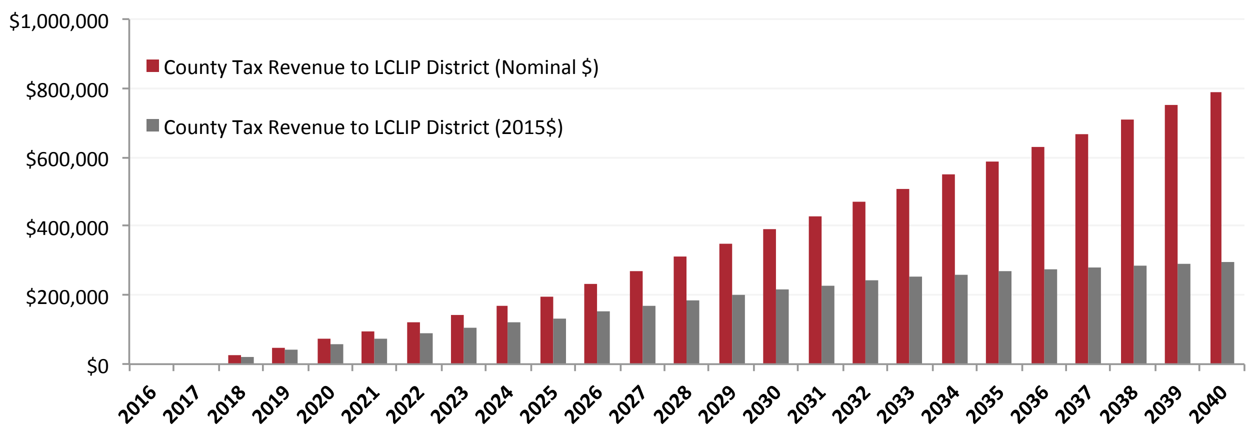
LCLIP would produce significant funding benefits to the City. Assuming a 100% specified ratio (City commits to all 231 credits), total revenue to the City from the County's portion of property tax revenues would be $4.4 million (net present value, $8.5 million in nominal terms) over the 25-year period and reach about $300,000 annually (in 2015 dollars, nearly $800,000 in nominal terms) by year 25 of the program.

Exhibit 11. Scenario 2 Summary

Total Square Feet of Growth	3.7 Million Square Feet	
TDR Credits Used	231	
Revenues	2015 Dollars (Inflation Adjusted)	Nominal (Non-Inflation Adjusted)
Total LCLIP Revenues	$12.0 Million	$22.8 Million
City Portion of Property Tax	$7.6 Million	$14.3 Million
County Portion of Property Tax	$4.4 Million	$8.5 Million
City TDR Acquisition Cost	$0	$0
City Net Revenue	**$4.4 Million**	**$8.5 Million**

Source: ECONorthwest. Note all figures in 2015 dollars; 25-year present value at 4% discount rate

Exhibit 12. Scenario 2 Annual LCLIP Revenues



Source: ECONorthwest

Scenario 3: High Growth with Full MFTE Program

The High Growth scenario tests the revenue potential if the City realizes more development than planned for under the City's growth target. This scenario assumes the City realizes over 5.4 million square feet of new development by 2040, which represents 61 percent of PSRC's 2035 growth target for the City. This growth is significantly more development than historically experienced and the 3.7 million square feet assumed in Scenario 1. As with Scenario 2, this scenario assumes that the eight-year MFTE program is enacted for the entire the Study Area at the start of the program.

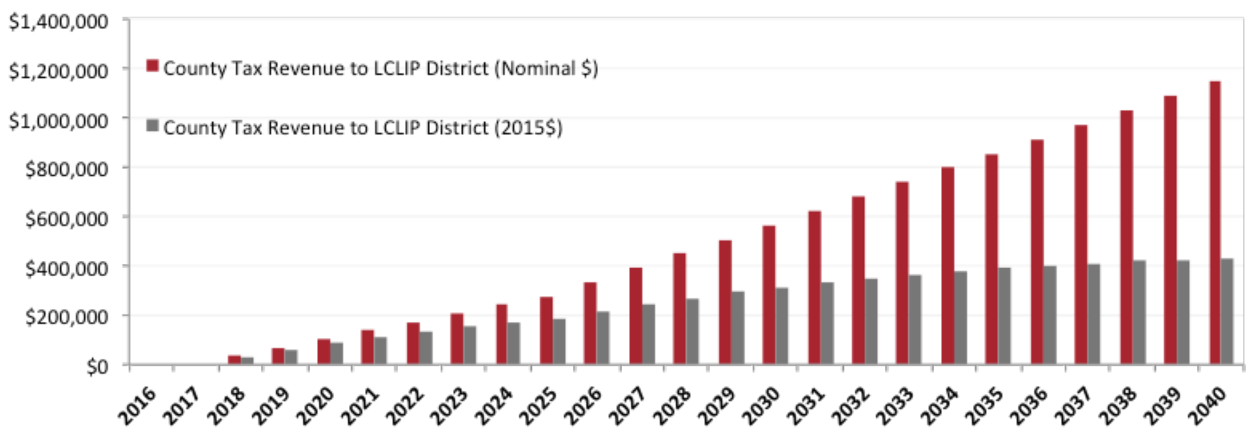
Under these assumptions the private market would be able to place all of the City's 231 TDR credits and meet each performance threshold without public support. Assuming a 100% specified ratio (the City commits to all 231 credits), the program could generate $7.3 million (net present value, $13.9 million in nominal terms) over the 25-year period and reach over $400,000 annually (in 2015 dollars, $1.3 million in nominal terms) by year 25 of the program.

Exhibit 13. Scenario 3 Summary

Total Square Feet of Growth	5.4 Million Square Feet	
TDR Credits Used	231	
Revenues	2015 Dollars (Inflation Adjusted)	Nominal (Non-Inflation Adjusted)
Total LCLIP Revenues	$19.7 Million	$37.4 Million
City Portion of Property Tax	$12.4 Million	$23.4 Million
County Portion of Property Tax	$7.3 Million	$13.9 Million
City TDR Acquisition Cost	$0	$0
City Net Revenue	**$7.3 Million**	**$13.9 Million**

Source: ECONorthwest. Note all figures in 2015 dollars; 25-year present value at 4% discount rate

Exhibit 2. Scenario 3 Annual LCLIP Revenues



Source: ECONorthwest

Summary

The three most important factors influencing the success of LCLIP in Shoreline are the amount of growth occurring, the timing of that growth, and the number of TDR credits placed. In order for LCLIP to generate the projected revenues through the MFTE approach outlined here, Shoreline will need to locate at least half of its PSRC growth target within the Study Area over the timeframe of the program.

In addition to the amount of development projected, high utilization of the MFTE incentive in projects within the Study Areas will be an important factor in ensuring the City consistently meets its TDR placement milestones and increases the assessed value for revenue purposes. As a result, the City will want to establish an exchange rate that provides sufficient incentive for developers to use the tool. Other factors, such as timing the start of the program and choosing how many credits to accept will influence the success of LCLIP in Shoreline.

5 LCLIP Program Findings and Recommendations

5.1 Summary of Findings

There is strong policy case for LCLIP in Shoreline.

The Study Area, including Town Center, Aurora Square, and the future light rail station areas, will play a central role in the city meeting its growth targets. These areas will have the capacity to accommodate considerable new population and employment. Residential capacity, particularly in the light rail station areas, can use TDR (and, by extension, generate LCLIP funding) through use of the multi-family tax exemption program. The study area can benefit from infrastructure improvements to support redevelopment, especially around improving access to transit. Flexible funding from LCLIP can provide Shoreline with a revenue source to help make those investments. A moderate growth scenario could generate $4.4 million (net present value, $8.5 million in nominal terms) while a more aggressive growth scenario could generate $7.3 million (net present value, $13.9 million in nominal terms).

A market-driven approach to TDR placement can make LCLIP viable.

Shoreline recently adopted a subarea plan for the 185th Street light rail station area. This plan contains provisions for market-based use of TDR, which can serve as a cornerstone for TDR use in the City. By itself, the 185th Street light rail station area will not place enough credits to make LCLIP successful, but if Shoreline can expand use of TDR in other areas the picture changes. By extending the MFTE program to other parts of the City the private market can absorb enough TDR credits to meet the LCLIP performance milestones.

Furthermore, Shoreline can augment the MFTE approach by negotiating TDR use as part of development agreements for projects in Aurora Square. This mechanism is variable and the scale of future Aurora Square projects is uncertain, however the inclusion of TDR as part of future projects in the Community Renewal Area could help accelerate the City's TDR placement and contribute to revenues. The pursuit of development agreements in Aurora Square should be a focus for the City as an opportunity throughout the duration of the LCLIP timeline or as a catalyst for the start of the program.

The timing of redevelopment is a key to the success of LCLIP.

Current conditions in Shoreline may not present a strong case for starting LCLIP immediately, however important zoning changes around the future light rail station areas create an important opportunity for redevelopment. New projects are already emerging in Town Center and the potential for redevelopment in Aurora Square is another potential driver for LCLIP success. In order to maximize revenues and mitigate risks the City may time the use of LCLIP around known projects that would use TDR.

5.2 Recommendations

Shoreline can pursue a range of actions to maximize the benefits of LCLIP while reducing its exposure to the risks of not meeting performance milestones. The City can take an approach to using the program that combines strategic and opportunistic elements. In thinking about using LCLIP, the City should consider a suite of actions that collectively could create conditions for the program to succeed.

Potential LCLIP Approaches

The follow section lays out three approaches to proceeding with LCLIP.

No Action in the Immediate Future

The analysis shows that while the 185th Street subarea can retire nearly one third of the City's allocation of development rights, by itself this source of demand will not be sufficient to meet the performance milestones of the program over time. Pursuing LCLIP under the status quo would either require City acquisition of credits to keep the revenue flowing or would result in the premature conclusion of the program without City acquisitions to bridge the gap.

Furthermore, Shoreline will soon consider a rezone of the 145th Street light rail station area, the outcome of which could potentially create more opportunities for using LCLIP. While the City may not consider adoption of LCLIP prior to the completion of the 145th Street subarea plan, it could strengthen the viability of LCLIP by including provisions in the rezone that support its use.

Target Maximum Specified Portion

This approach would establish LCLIP targeted at placing all 231 credits allocated to Shoreline. The program is designed to provide greater financial incentives for cities accepting higher numbers of credits. This would maximize revenue to the City but also carries increased risk as the program could end early (or require City intervention) should growth and TDR use not keep pace with performance milestones. King County has expressed a willingness to incorporate flexibility into a potential LCLIP partnership with Shoreline in ways that would reduce the City's financial exposure. This approach is predicated on the location of at least half of Shoreline's PSRC growth target within the four potential LCLIP districts identified in the analysis.

Time and calibrate LCLIP program to a development/TDR milestone(s).

The city can structure the start of the LCLIP program with a single (or multiple) major development, such as a project in Aurora Square or a multifamily/mixed-use project in either Town Center or a light rail station area. Timing the program to the start of a known large-scale development within the City would create three advantages. Shoreline could capitalize on known demand, increase the program benefits, and reduce risk by making progress towards performance milestones from the outset of the program.

Tying the program to a known quantity of TDR use would allow the city to comfortably structure the LCLIP program to run for the full 25 years (i.e. meet performance thresholds). Making headway on the performance thresholds in advance would allow the City more flexibility on the use of funds by allowing some public infrastructure costs to be financed with debt, should that be desirable.

Summary recommendations for path to LCLIP implementation

- Commit to all 231 credits to maximize revenues.
- Include 25% of the City's assessed value in the program by incorporating all four areas (Aurora Square, Town Center, and both light rail station areas), and expanding the Town Center LCLIP district.
- Consider including an incentive zoning provision in the 145th Street subarea plan or a MFTE provision similar to that adopted in the 185th Street subarea plan.
- Extend the MFTE provision for TDR use across all potential LCLIP districts (185th is already in place).
- Pursue TDR use as part of development agreements for Aurora Square projects.
- Discuss flexibility and accommodations around program performance milestones with King County.
- Prepare all the groundwork for adoption of LCLIP so the City may start the program on short notice as conditions change.
- Time the start of the program in conjunction with a project that would use TDR.

Furthermore, in moving forward the City should monitor the following conditions:

- Indications that confirm market interest in TDR, such as development applications that have been or are expected to be proposed that will need TDR credits in different zones.
- Analysis of the expected use of TDR credits confirms a reasonably high likelihood of meeting threshold requirements for TDR use in the LCLIP district.
- Infrastructure projects have been identified that qualify under the LCLIP program.
- A LCLIP district can be created that maximizes the projected LCLIP revenue to pay for infrastructure projects while meeting the requirements of the LCLIP legislation.
- As needed, a shared strategy approach with King County or another partner agency should be included in an approach to retiring TDR credits.

6 Implementation Road Map

Should the city of Shoreline choose to pursue LCLIP, the following next steps are necessary to implement the program:

Step 1: Identify a specific geographic area for increased density that will become a local infrastructure project area ("LIPA"). The LIPA must:

- Include contiguous land (no "islands" within a LIPA)
- Not include more than 25% of the total assessed taxable property within the city
- Not overlap another LIPA
- In the aggregate, be of sufficient size to: 1) use the City's "specified portion" of transferable development rights (unless the City has purchased the transferable development rights to reserve for future development), and 2) not be larger than reasonably necessary
- Contain all public improvements to be financed within its boundaries

Step 2: Accept responsibility for all or a share (a "specified portion") of the transferable development rights allocated from the Puget Sound Regional Council to the city. Consider whether to include any rights from another city through an interlocal agreement.

Step 3: Adopt a plan for development of public infrastructure within the LIPA. The plan must:

- Utilize at least 20% of the city's allocated share of transferable development rights
- Be developed in consultation with the Department of Transportation and the county where the LIPA is located
- Be consistent with any transfer of development rights policies or development regulations adopted by the city
- Specify the public improvements that will be financed
- Estimate the number of transferable development rights that will be used
- Estimate the cost of the public improvements

Step 4: Adopt transfer of development rights policies or implement development regulations, <u>or</u> make a finding that the city will receive its specified portion within one or more LIPAs, <u>or</u> make a finding that the city will purchase its specified portion. Adoption of transfer of development rights policies or implementation of development regulations must:

- Comply with the Growth Management Act
- Designate a receiving area(s)
- Adopt developer incentives, which should be designed, at the City's election, to:
- Achieve the densities or intensities in the City's plan
- Include streamlined permitting strategies
- Include streamlined environmental review strategies
- Establish an exchange rate, which should be designed to:
- Create a marketplace where transferable development rights can be bought and sold
- Achieve the densities or intensities in the city's plan

Provide for translation to commodities in addition to residential density (e.g., building height, commercial floor area, parking ratio, impervious surface, parkland and open space, setbacks and floor area ratio)

Allow for appropriate exemptions from land use and building requirements

- Require that the sale of the transferable development rights be evidenced by its permanent removal from the sending site (such as through a conservation easement on the sending site)
- Not be based on a downzone within the receiving area

The City may elect to adopt optional comprehensive plan element and optional development regulations that apply within the LIPA

Step 5: Hold a public hearing on the proposed formation of the LIPA. Notice must be provided to the county assessor, county treasurer, and county within the proposed LIPA of the City's intent to create the area. Notice must be provided at least 180 days in advance of the public hearing.

Step 6: Adopt an ordinance or resolution creating the LIPA. The ordinance or resolution must:

- Describe the proposed public improvements
- Describe the boundaries of the proposed LIPA
- Provide the date when the use of local property tax allocation revenues will commence and a list of the participating tax districts (the city and county)

A certified copy of the adopted ordinance or resolution must be delivered to the county assessor, county treasurer and each participating tax district

Step 7: Provide a report along with the county to the Department of Commerce by March 1st of each year. A requirement of participating in the LCLIP program is for Counties in cooperation with cities, to provide the Department of Commerce with a report on March 1st of every other year. Should the City of Shoreline choose to participate, the City in cooperation with King County would compile a report containing the following information:

- Number of cities within the county participating in LCLIP; and,
- The number of TDR transactions that have occurred; and,
- The number of acres conserved through the program, broken out by land type, agricultural, forest, or rural; and,
- The number of TDR credits transferred; and,
- The number of TDR credits transferred into the cities; and,
  - The total number of new residential units in the city; and,
  - The number of additional residential units allowed due to TDR credit transfers; and,
  - The amount of additional commercial space allowed due to TDR credit transfers; and,
  - The amount of additional building height allowed due to TDR credit transfers; and,
  - The amount of structured parking spaces reduced due to TDR credit transfers; and,
  - The amount of additional parking spaces allowed due to TDR credit transfers; and,
  - The amount of additional impervious surface allowed due to TDR credit transfers; and,
- The amount of property tax revenues per city received from the county; and,

- A list of public improvements paid for or financed by the received revenues; and,
- The names of businesses locating within the district as a result of the public improvements; and,
  - The number of permanent jobs created in the district as a result of the public improvements; and,
  - The average wages and benefits received by the employees; and,
- The date at which any indebtedness issued for LCLIP financing is expected to be retired.

Council Questions from July 20, 2015 Council Discussion

The following questions were raised by Councilmembers during the presentation and discussion on LCLIP on July 20, 2015. Most of the questions that the Councilmembers asked had to do with financial risk, benefits to the City, and how much additional property tax would the City receive as a result of implementing the program while deducting the amount of property tax that would not be collected on developments approved for MFTE. Specific questions and comments are listed below:

1. What are the incentives for developers to purchase TDR credits?

   The City would need to create the incentive for developers. This could come in the form of allowing greater development potential than currently allowed or foregoing other requirements, such as affordable housing requirements for developers who purchase the TDR credits.

2. What's the trade-off of waiving the requirement for affordable housing for the first 300-units?

   Delay of Council's goal for more affordable housing, particularly in the Station Areas.

3. What would a property owner have to pay over a 25-year period? Consider an 8-year MFTE and the cost of buying TDR credits.

   Using the example from Forterra (discussed on p. 15 of Attachment B), the developer of a 120 unit development granted an 8-year MFTE would buy 5 TDR credits at a cost of $106,000 to $114,000 per year offset by the property tax exemption savings of $163,000 to $175,000 per year it is receiving the 8-year MFTE. The end result is the developer has purchased 40 TDR credits (at a ratio of 1 TDR credit per 3 units) at a cost of approximately $0.88 million offset by property tax exemption savings of $1.35 million, thereby resulting in a net savings of $0.47 million. For the remaining length of the LCLIP the property owner would pay the same property tax as they would have without the MFTE.

Exhibit 4. TDR Credits to Access MFTE Program

		Annual Tax Δ	Split		
		1%	65%	TDR Cost:	$20,000
				Inflation:	2%
	Year	MFTE Benefit	TDR Contribution	Project Tax Savings	TDR Credits Afforded
1	2015	$163,200	$106,080	$57,120	5.2
2	2016	$164,832	$107,141	$57,691	5.1
3	2017	$166,480	$108,212	$58,268	5.1
4	2018	$168,145	$109,294	$58,851	5.0
5	2019	$169,827	$110,387	$59,439	5.0
6	2020	$171,525	$111,491	$60,034	5.0
7	2021	$173,240	$112,606	$60,634	4.9
8	2022	$174,972	$113,732	$61,240	4.9
	Total	$1,352,221	$878,944	$473,278	40.2
	NPV	$967,464	$628,852	$338,612	

MFTE Property Tax Exemption Value

Cost of TDR Credits

Net Project Savings:

4. How does this program work and where do the taxes go?

   If the City meets its obligations under the LCLIP program, then the King County Assessor's Office will calculate the property tax allocation revenue value for the Local Infrastructure Project Area (LIPA). This is an amount equal to the sponsoring city ratio multiplied by 75% of any increase in the assessed value of real property in the LIPA resulting from new construction placed on the assessment roll applied to the then current City regular levy rate and King County current expense levy rate. King County then directs a portion of its property tax to the City and identifies the portion of the City's property tax to be used to fund infrastructure projects within the identified LCLIP district.

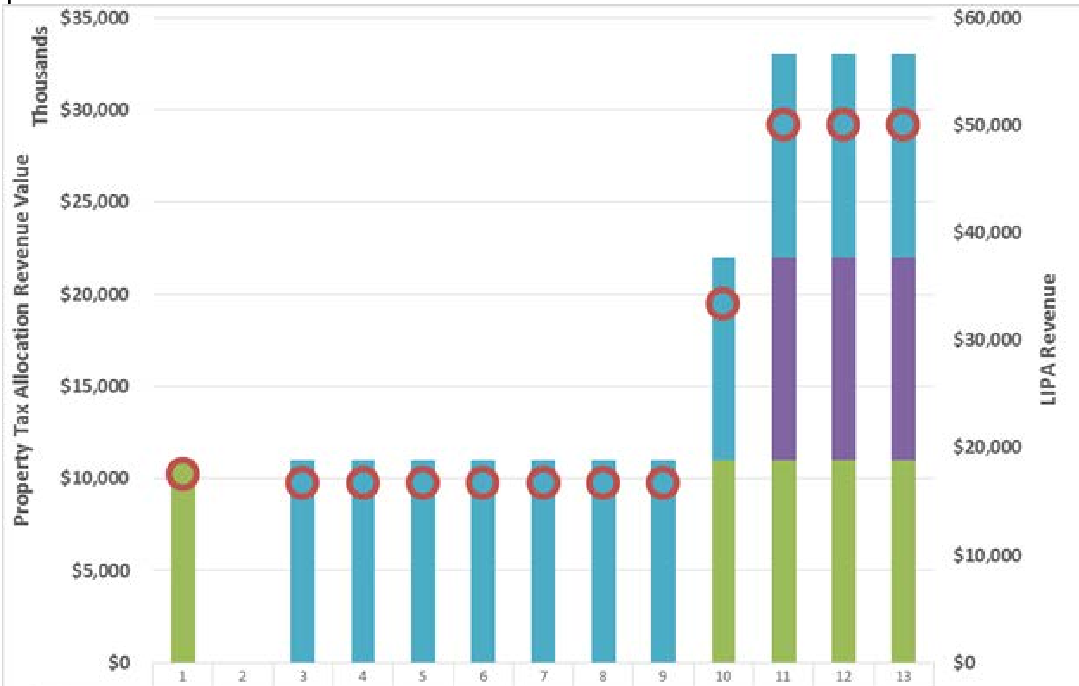
   The chart below exhibits a simple example calculation for four projects coming online within a 13-year period. For this example let's assume that the LCLIP program only runs for a 13-year period (any additional years makes the chart illegible), each of the four projects will have an assessed value of $11.0 million, and the City offers a 8-year MFTE.

   Example 1: The Abracadabra is constructed in year 1 of the LCLIP program. The LIPA calculation for year 1 captured the value of that new construction. The property was granted a MFTE in year 2. The new construction value is not captured in LIPA calculations for years 2 through 9 until the MFTE expires at the end of year 9 and the value of the new construction (unadjusted from its year 1 value) is placed back on the assessment roll in year 10. The LIPA calculation for years 10 through 13 will capture the value of that new construction.

   Example 2: The Palomino is constructed in year 3 of the LCLIP program and is granted a MFTE before the value of the new construction is placed on the assessment roll. The new construction value is not captured in LIPA calculations for years 3 through 10 until the MFTE expires at the end of year 10 and the value of the new construction (unadjusted from its year 3 value) is placed back on the assessment roll in year 11. The LIPA calculation for years 11 through 13 will capture the value of that new construction.

   Example 3: The Monumental is constructed in year 3 of the LCLIP program. This project did not apply for a MFTE so all of its new construction value was placed on the assessment roll and is captured in LIPA calculations for years 3 through 13.

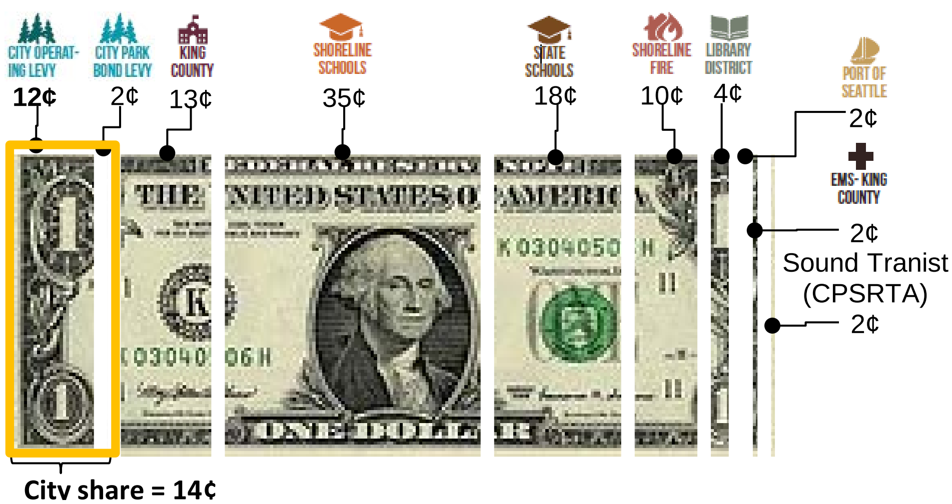
   Example 4: The Shoreline Edge is constructed in year 6 of the LCLIP program and is granted a MFTE before the value of the new construction is placed on the assessment roll. The new construction value is not captured in LIPA calculations for years 6 through 13 because it is not placed on the assessment roll until the MFTE expires at the end of year 13. Essentially this example illustrates that there is risk to offering a MFTE. Any project granted a MFTE that prevents the value of new construction from being placed on the assessment roll within the LCLIP program's defined period (again, in this example it is 13 years) will not be captured in the LIPA calculation.



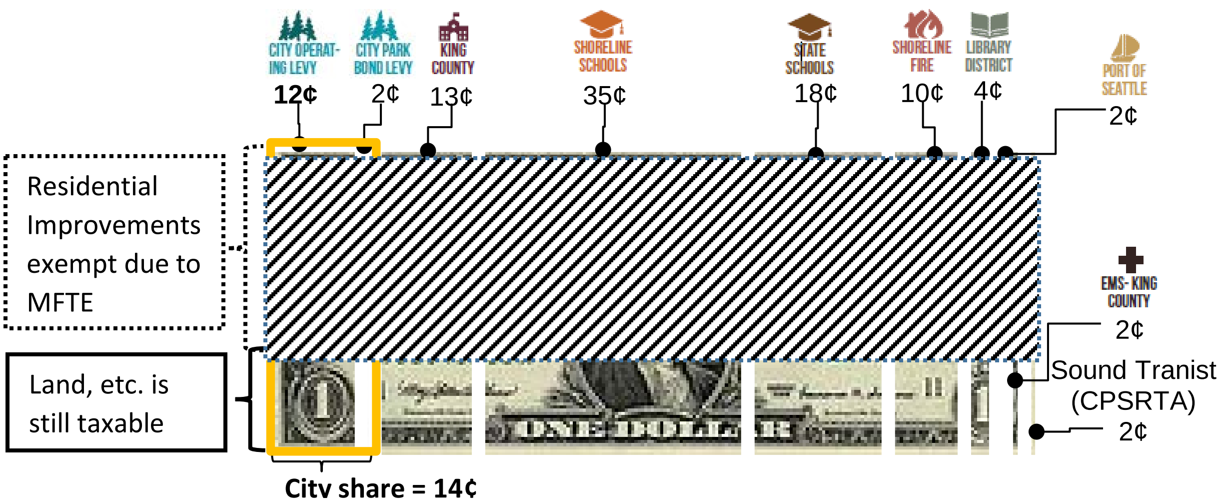
	1	2	3	4	5	6	7	8	9	10	11	12	13
Shoreline Edge	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Monumental	$0	$0	$11,000	$11,000	$11,000	$11,000	$11,000	$11,000	$11,000	$11,000	$11,000	$11,000	$11,000
Palomino	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$11,000	$11,000	$11,000
Abracadabra	$11,000	$0	$0	$0	$0	$0	$0	$0	$0	$11,000	$11,000	$11,000	$11,000
Total LIPA	$17,490		$16,665	$16,665	$16,665	$16,665	$16,665	$16,665	$16,665	$33,330	$49,995	$49,995	$49,995

5. Provide a chart of what a property owner would pay over 25-years, to whom, with MFTE implemented on the parcel.

   Property owners currently pay taxes on the taxable assessed value of land and improvements to nine taxing jurisdictions as shown in the chart below.



A property owner granted a MFTE will be exempt from paying property tax to all jurisdictions on the portion of the assessed value of the residential improvements alone. The tax exemption does not apply to land, retail space, other commercial space, or any residential units that were in existence at the time of application.



It is important to note that the timing of the City issuing the Final Certificate for tax exemption to the King County Assessor's Office (KCAO) is of importance. If the certificate is issued before any new construction comes on the tax roll, the City's levy (and others including the school district, fire district, etc.) does not grow until the MFTE expires and the value of new construction comes on the tax rolls in the following year. This is important because if the value of new construction comes on the tax rolls before the MFTE is granted, thereby growing the levy, the property owner will receive relief from paying property tax but the burden is shifted to all remaining taxpayers to pay the full amount of the levy. When the property's MFTE expires the burden is then shared again by the property owner.

6. What is the financial impact to the City? Consider 8-MFTE combined with a portion of King County's taxes going back into infrastructure projects.

   The financial impact to the City culminates in less general revenue to support increased demand for operating programs (such as recreation programming, police services, etc.) as up to (or whatever the sponsoring city ratio is depending on how many of the 231 credits the City chooses to place) of the value of the new construction, or approximately $7.6 million in property tax revenue if the City accepts responsibility to place all 231 credits, in the LCLIP district is dedicated to funding infrastructure projects sited within the LCLIP district.

7. Will a developer have a choice of an 8-year MFTE or a 12-year PTE for affordable units?

   Currently only a 12 year PTE is available. Council could adopt an 8 year version.

8. What are the penalties for stopping the program?

   The City is obligated to meet thresholds that it agrees to at the beginning of the program. If developers don't purchase the credits then the City will be required to purchase them in order to meet the thresholds if the City wants to continue to collect King County's portion of property taxes. If the City fails to meet any of the thresholds, KCAO will no longer perform the LIPA calculation described in the response to question 3 or distribute property tax allocation revenue.

9. What are other incentives to offer developers in order for the City to meet TDR obligations?

   Possible incentives and strategies to sell TDR credits were detailed in the staff report beginning on page 5.

10. Why in the first 10-years of the program is very little money generated?

    In the first 8 years the projects sited within the LCLIP districts would likely apply for a MFTE that could prevent a portion or all of the value of new construction from coming on the rolls, in which event that value is not be captured in the LIPA calculation until the MFTE expires.

11. Would an 8-year MFTE only apply for developers who buy TDR's?

    This would be an incentive option that the City could offer.