CHAPEL HILL LUMO UPDATE

Feasibility of Code-Based Incentives to Support Community Benefits

April 4, 2024

SBFRIEDMAN

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LUMO Update

Feasibility of Code-Based Incentives to Support Community Benefits

October 2023 Findings

- At minimum, a 50% density bonus is needed for a project with a 15% affordability set aside to achieve financial returns comparable to a lower density project without any set aside
- To be attractive, a voluntary density bonus would need to provide significantly higher returns than the base scenario
- A 50%+ density bonus would likely require more expensive construction techniques
- In the Chapel Hill market, the hard cost premium associated with concrete framing exceeds achievable rent premiums; thereby limiting the attractiveness of density bonuses

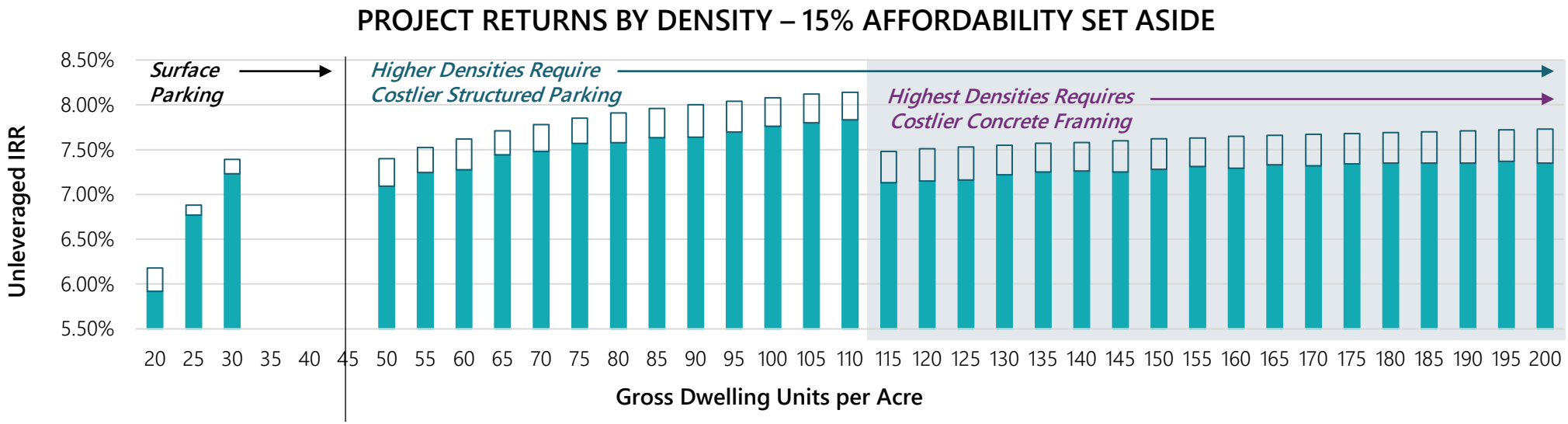
January-March 2024 – Financial Testing

1. Testing different affordability requirements to understand density bonuses needed to offset impact to revenues
2. Testing extent by which of setback and buffer modifications can support additional project costs to fund community benefits
    - Street setback modification
    - RCD buffer modification
3. Testing minimum number of rental townhome and missing middle units needed to support Town's affordability set aside targets

Density Analysis

Density Analysis

Density bonus needed to return to baseline returns at various DUs/acre



Wood Frame Construction, Structured Parking

Base DU/Acre	DU/Acre to Achieve Similar Returns	**Density Bonus to Achieve Similar Returns**
50	*65*	***30%***
55	*75*	***36%***
60	85	**42%**
65	95	**46%**
70	105	**50%**

Affordability Requirements

Affordability Requirements

Testing density bonus needed to offset impact to revenues

Wood Frame Construction, Structured Parking	Unit Breakdown				Weighted Average NOI/Unit	Impact to NOI/Unit	Density Bonus to Achieve Similar Returns
	Market Rate	80% AMI	65% AMI	60% AMI			
NOI	$17,790	$16,682	$13,051	$11,575			
No affordability set aside	*100%*				*$17,790*		
7.5% of units at 65% AMI & 7.5% of units at 80% AMI	*85.0%*	*7.5%*	*7.5%*		*$17,351*	*-$439*	***50%***
7.5% of units at 60% AMI	92.5%			7.5%	$17,324	-$466	**50%**
5% of units at 65% AMI & 5% of units at 80% AMI	90.0%	5.0%	5.0%		$17,498	-$292	**25%**
15% of units at 80% AMI	85.0%	15.0%			$17,624	-$166	**20%**
3.5% of units at 60% AMI	96.5%			3.5%	$17,572	-$218	**20%**

[1] Density bonus could be reflected in an increase in height or increase in net developable land area

Cost of Affordability Requirements

Estimating subsidies needed at various AMIs to return to baseline market rate returns

Wood Frame Construction, Structured Parking		Market Rate	80% AMI	65% AMI	60% AMI
NOI/unit		$17,790	$16,682	$13,051	$11,575
Value per unit at a 5.7% cap		*$312,000*	*$293,000*	*$229,000*	*$203,000*
Reduction in value per unit			*6.2%*	*26.6%*	*34.9%*
Yield on cost per unit	$300,000/unit TDC	*5.9%*	*5.6%*	*4.4%*	*3.9%*
Estimated subsidy to return to baseline market rate returns *(Holding constant the relationship between TDC & valuation)*			$19,000	$80,000	$105,000
Yield on cost per unit after subsidy		5.9%	5.9%	5.9%	5.9%

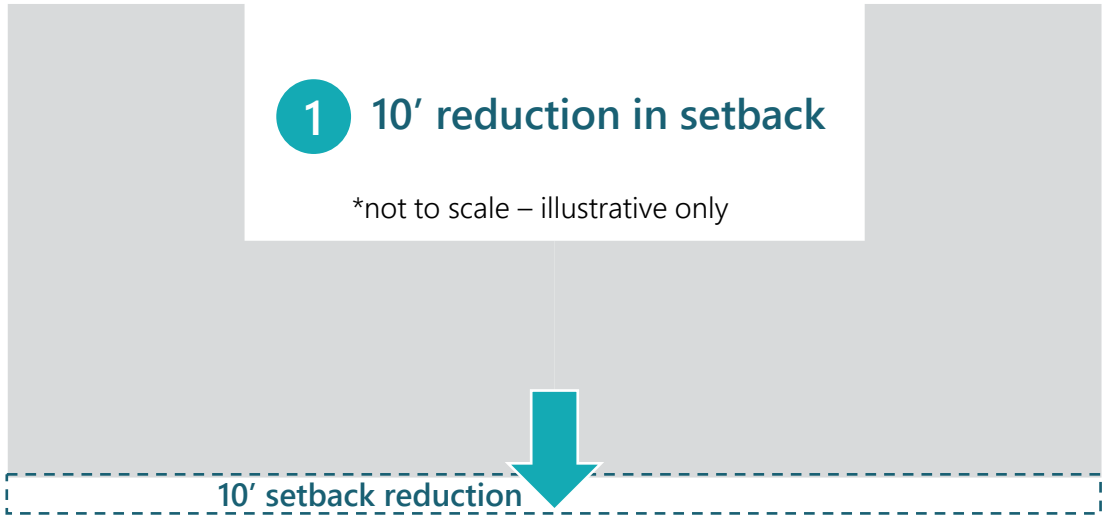
Street Setback Modification

Street Setback Modification

Testing extent by which reduced street setback can support community benefits

- Existing R5 & R6 Zoning Districts require **20’ minimum** street setback
- Updated LUMO Update is considering **10’ minimum**

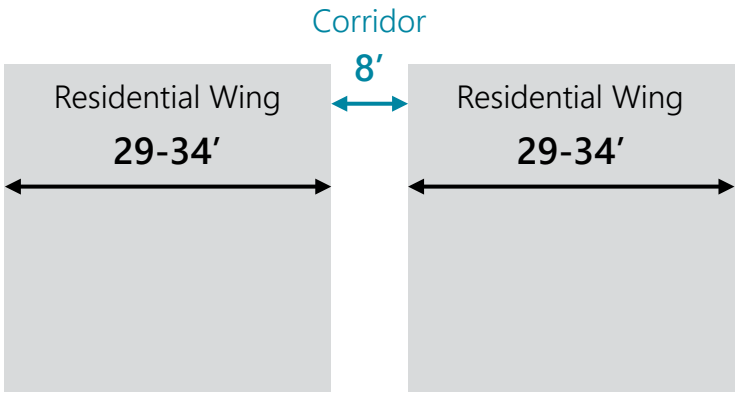
- Chapel Hill multifamily is largely double-loaded corridors in residential wings
- Value of reduced setback comes from allowing additional development at the end of residential wings
- Developers likely will not value greater unit depth



Street Setback Modification

Testing extent by which reduced street setback can support community benefits

- Typical depth of residential wings in Chapel Hill: **65-75'**
- Estimated width of interior corridors: **8'**
- Estimated unit depth: **29-34' (31' average)**



- 31' (depth) x 20' (width) x 2 (assumed residential wings) x 6 (assumed floors) = **7,440 of additional RSF**
- One potential configuration:

Unit Type	Assumed SF	Additional Units	Additional SF
Studio	625	4	2,500
1-bedroom	760	5	3,800
2-bedroom	1,150	1	1,150
3-bedroom	1,425		
Total		10	7,450

Street Setback Modification

Testing extent by which reduced street setback can support community benefits

- Assuming baseline 75 DUA project, $20/land SF acquisition cost, no baseline affordability

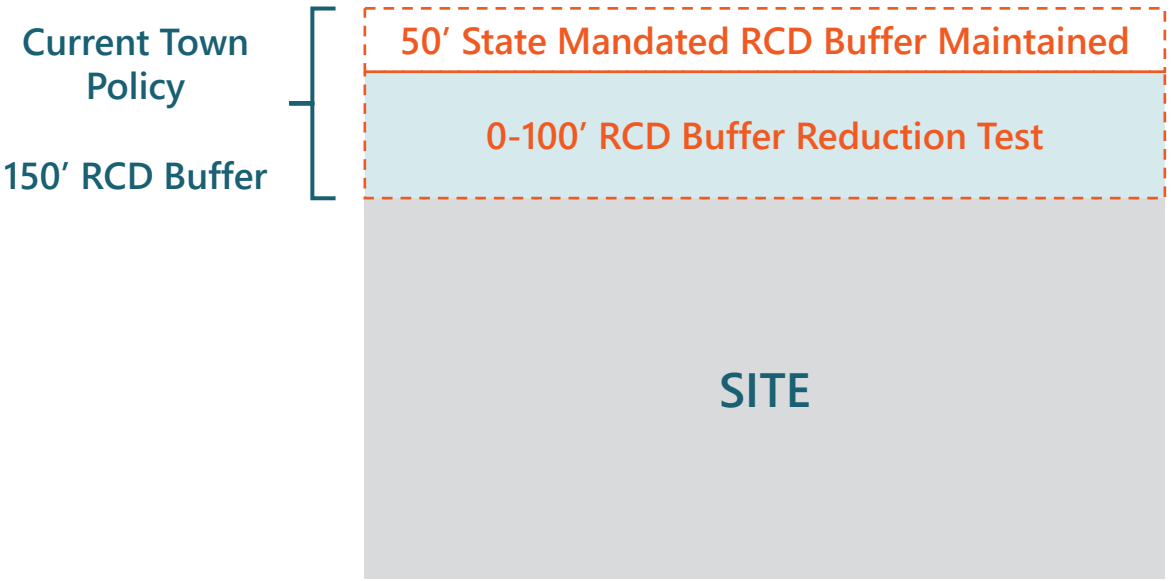
	Baseline	Sensitivity
Total Units	225	235
Density	75 DUA / 1.84 FAR	78 DUA / 1.91 FAR
Total Project Cost	$64,850,586	$67,093,394
Cost per Unit	$288,225	$285,504
Yield on Cost	6.19%	6.21%
Benefit to Project over Baseline / Supportable Community Benefits [1]	--	**$262,000**
per Additional Unit		**$26,000**
as a Percent of Additional Unit Per-Unit Cost		**9.2%**

[1] Estimated community benefits that could be supported by the project while maintaining baseline developer returns

RCD Buffer Modification

RCD Buffer Modification

Testing extent by which reduced RCD buffer can support community benefits



- Benefit of an RCD buffer modification will vary based on site characteristics

RCD Buffer Modification

Testing extent by which reduced RCD buffer can support community benefits

- Assuming baseline 90 DUA project, $20/land SF site acquisition cost, no baseline affordability
- Baseline site is assumed to have a net developable area of 435' (width) x 200' (depth)
- Reduction in the RCD buffer increases the depth of the developable area
- Assuming site acquisition costs remain constant as previously undevelopable land becomes developable

	Baseline	25' Reduction	50' Reduction	75' Reduction	100' Reduction
RCD Buffer	150'	125'	100'	75'	50'
Net Developable Area (AC)	2.0	2.25	2.50	2.75	3.00
Density	90 DUA	--	--	--	--
Total Units	180	202	225	247	270
Total Project Cost / Unit	$284,160	$283,632	$282,807	$281,653	$281,264
Yield on Cost	6.26%	6.29%	6.31%	6.32%	6.34%
Benefit to Project over Baseline / Supportable Community Benefits [1]	--	**$196,700**	**$423,900**	**$645,300**	**$862,100**
per Additional Unit		**$8,900**	**$9,400**	**$9,600**	**$9,600**
as a Percent of Additional Unit Per-Unit Cost		**3.2%**	**3.3%**	**3.4%**	**3.4%**

[1] Estimated community benefits that could be supported by the project while maintaining baseline developer returns

‘How Small?’ Assessment

‘How Small?’ Rental Assessment

1 unit at 65% AMI & 1 unit at 80% AMI

Testing minimum number of TH or MM units needed to support Town’s affordability set aside targets

Site Acquisition Cost: $5/Land SF		Hurdle Rate	10 units	12 units
Rental Townhomes 1 unit at 65% AMI & 1 unit at 80% AMI	Stabilized Yield on Cost	5.9%	5.87%	6.11%
	Unleveraged IRR	7.0%	7.18%	7.68%
Rental Missing Middle 1 unit at 65% AMI & 1 unit at 80% AMI	Stabilized Yield on Cost	5.9%	5.73%	5.95%
	Unleveraged IRR	7.0%	6.88%	7.35%

Ability to carry affordable units is highly dependent on the site acquisition costs.

With acquisition costs of $5/SF land, a **minimum of 12 units** appear to be required to carry 2 units at the Town’s current affordability target.

This results in a 16.6% set aside.

‘How Small?’ Rental Assessment

1 unit at 65% AMI & 1 unit at 80% AMI

Testing minimum number of TH or MM units needed to support Town’s affordability set aside targets

Site Acquisition Cost: $10/Land SF		Hurdle Rate	10 units	12 units	14 units	16 units
Rental Townhomes 1 unit at 65% AMI & 1 unit at 80% AMI	Stabilized Yield on Cost	5.9%	5.58%	5.85%	6.09%	
	Unleveraged IRR	7.0%	6.56%	7.14%	7.66%	
Rental Missing Middle 1 unit at 65% AMI & 1 unit at 80% AMI	Stabilized Yield on Cost	5.9%	5.49%	5.73%	5.89%	6.04%
	Unleveraged IRR	7.0%	6.37%	6.9%	7.23%	7.54%

Ability to carry affordable units is highly dependent on the site acquisition costs.

With acquisition costs of $10/SF land, a **minimum of 14-16 units** appear to be required to carry 2 units at the Town’s current affordability target.

This results in a 12.5-14.3% set aside.

‘How Small?’ Rental Assessment

1 unit at 60% AMI

Testing minimum number of TH or MM units needed to support one unit at deeper affordability

Site Acquisition Cost: $5/Land SF		Hurdle Rate	10 units	12 units
Rental Townhomes 1 unit at 60% AMI	Stabilized Yield on Cost	5.9%	5.87%	6.11%
	Unleveraged IRR	7.0%	7.18%	7.69%
Rental Missing Middle 1 unit at 60% AMI	Stabilized Yield on Cost	5.9%	5.67%	5.90%
	Unleveraged IRR	7.0%	6.76%	7.24%

Ability to carry affordable units is highly dependent on the site acquisition costs.

With acquisition costs of $5/SF land, a **minimum of 12 units** appear to be required to carry 1 unit at a 60% AMI affordability target.

This results in an 8.3% set aside.

‘How Small?’ Rental Assessment

1 unit at 60% AMI

Testing minimum number of TH or MM units needed to support one unit at deeper affordability

Site Acquisition Cost: $10/Land SF		Hurdle Rate	10 units	12 units	14 units	16 units
Rental Townhomes 1 unit at 60% AMI	Stabilized Yield on Cost	5.9%	5.58%	5.85%	6.10%	
	Unleveraged IRR	7.0%	6.57%	7.15%	7.66%	
Rental Missing Middle 1 unit at 60% AMI	Stabilized Yield on Cost	5.9%	5.44%	5.69%	5.85%	6.00%
	Unleveraged IRR	7.0%	6.24%	6.79%	7.14%	7.46%

Ability to carry affordable units is highly dependent on the site acquisition costs.

With acquisition costs of $10/SF land, a **minimum of 14-16 units** appear to be required to carry 1 unit at a 60% AMI affordability target.

This results in a 6.3-7.1% set aside.

‘How Small?’ Sale Assessment

Testing minimum number of TH units needed to support one unit at deeper affordability

For-Sale Townhomes

Assumes: 3-bed, 1,950 SF units
Sale Prices: $525,000 for Market Rate, $138,000 for 65% AMI, $180,000 for 80% AMI

	1 unit at 65% & 1 unit at 80% AMI	1 unit at 65% AMI	1 unit at 80% AMI
Site Acquisition Cost: $5/Land SF	12 total units	10 total units	10 total units
Site Acquisition Cost: $10/Land SF	14 total units	12 total units	12 total units

Ability to carry affordable units is highly dependent on the site acquisition costs & market-rate sales price.

With acquisition costs of $5/SF land, a **minimum of 10-12 units** appear to be required to carry up to 2 units at the Town’s current affordability target.

With acquisition costs of $10/SF land, a **minimum of 12-14 units** appear to be required to carry up to 2 units at the Town’s current affordability target.

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