Is It a Funding Issue?

Economic Impacts of the Proposed City of Los Angeles Transfer Tax for Housing and Homelessness

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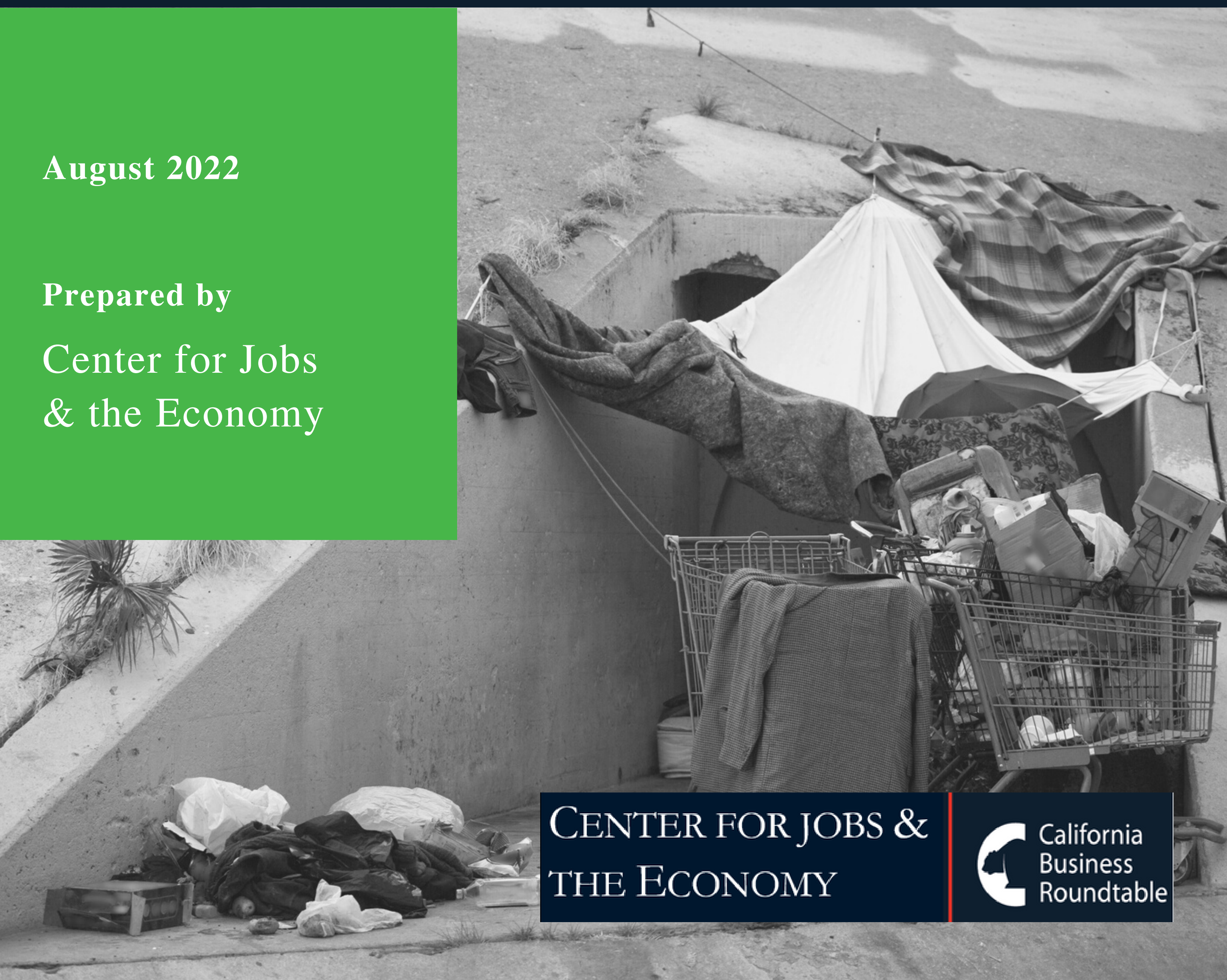
Prepared by

Center for Jobs & the Economy



CENTER FOR JOBS & THE ECONOMY

California Business Roundtable

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Introduction & Summary

The *Funding for Affordable Housing and Tenant Assistance Programs Through a Special Tax on Real Property Transfers Over $5 Million, Initiative Ordinance* (LA Transfer Tax) would impose a new tax of 4% on sales of properties valued at $5 to $10 million and 5.5% on property $10 million or more. With some changes, the measure would: (1) provide permanent funding for construction of affordable housing now being done through the Prop HHH bond measure approved by City voters in 2016, and (2) support homeless services largely comparable to those being funded through a ten-year, quarter cent sales tax approved by County voters in 2016.

If approved, this measure would be the largest tax increase in the City's history. At an estimated $860 million a year, the LA Transfer Tax would become the City's second largest tax source, behind only the general property tax. Compared to estimated revenues for 2022-23, the measure would represent a 27.3% increase in property taxes, and a 14.0% increase in total taxes charged by the City.

Contrary to the proponents' claims, only a small portion of the tax (28%) would be paid by "mega mansions" or single family homes. Just over two-thirds instead would be paid by business and rental properties. And while the measure is intended to "protect renters from rent hikes," the resulting price pressure on these properties will likely produce rent increases on both households and businesses of up to 5.5% to 8.0%. Rather than just "millionaires and billionaires," these costs will be paid by a broad range of household income levels and small businesses as the costs are passed on in higher rents and as the resulting price pressures affect rents throughout the City.

The measure covers a broad range of programs intended to address homelessness and low income renters. Half of the tax proceeds would go to construction and rehabilitation of affordable housing. Just under a quarter would go to income assistance and subsidies. The remainder would be split roughly between the administrative categories and to for grants to nonprofits—such as those listed as supporters of the measure—to provide social program and legal services.

The measure continues provisions that have hindered progress under the existing Prop HHH program, and in several instances adds other conditions and restrictions. Consequently, at current unit costs, the estimated $430 million from the new tax for housing would be sufficient to increase annual financing of affordable housing by only a net 640 units, or by an amount equivalent to a 0.04% increase in the City's housing supply. Using the average household size, this housing would accommodate 1,700 persons. This level would cover only 4% of the 41,290 homeless individuals identified in the 2020 surveys, or at a level that would not even maintain pace with the annual increase in the number of homeless. Given the unacceptably slow pace shown to date in the completion of the Prop HHH funded projects, the net 640 units does not necessarily mean new housing as it does additions to the current project backlog.

The problems in the current Prop HHH program—which are continued and expanded in the measure—have been assessed in a series of annual audits completed by the City Controller. In summary:

- The cost of funded projects has been too high, nearly double the levels assumed in the City's initial program plan. The most recent audit (February 2022) indicates that the average unit cost in 2021 was $596,846; 14% of units in construction are more than $700,000 per unit; and one project currently is estimated to cost almost $837,000 per unit. Looking at a broader range of affordable housing projects, State Treasurer data shows the cost of publicly funded affordable units in the City of Los Angeles soared 89% between 2016 when voters approved Prop HHH, to an average of $630,000 and a range $497,000 to $834,000 per unit in 2021.

- Projects are taking too long to complete, an estimated three to six years after funding award. The most recent audit indicates that more than half the funded units are not expected to be completed until after January 2023 or later, or more than six years after voters approved Prop HHH.

- Reasons cited for these high costs and delays include: (1) delays and added costs coming from the City's development review and housing regulations; (2) multiple financing sources for these projects that have their own approval process and conditions; (3) restricting funding only to developers with a record of affordable housing development, which limits the available developer, labor, and financing pool; and (4) higher labor costs and lower labor and subcontractor supply as the result of prevailing wage and project labor agreement (PLA) requirements.

The measure does not contain any reforms that would resolve the issues identified in the annual audits, and instead increases these restrictions including applying the PLA requirement to all new housing funded by this tax. The primary change is to eliminate the current Prop HHH public reviews of proposed project funding by two citizens committees, the City Council, and the Mayor. Project funding decisions instead are delegated to the Department of Housing, with a new Oversight Committee limited to program-level advice.

Conceptually, this funding is likely to support more than 640 new units a year by using the funds to leverage other sources, but 640 is the net addition made possible by the tax. Financing for publicly funded affordable housing primarily comes from federal, state, and foundation loans and grants, federal and state tax credits, and a range of mitigation funds coming from market rate developments. Although now experiencing an upsurge due to the federal pandemic assistance funds and the state surplus, these sources have been limited—the main driver behind the current effort by the nonprofit developers and other supporters of this measure to create a new funding source through a new tax. What leveraging that will be possible likely will still come from the same funding pool, an outcome that becomes even more likely given the measure's restrictions on eligible developers and the various provisions inflating the development costs.

As with any new tax, there will be an impact on jobs. Within Los Angeles County:

- Reduction in 4,000 direct and indirect jobs as business and rental properties pay the new tax.

- Uncertain effects on the estimated 33,100 direct and indirect jobs created by business and rental development investments near the threshold levels of the measure. Not all of these jobs would be eliminated, but just as likely would be shifted outside the City of Los Angeles. As development projects become more expensive compared to investment opportunities in adjacent areas, the broader Southern California, and other states, some projects could be delayed while others could still move forward but with changes based on revised project economics and scale. To the extent that investments move to other locations in the county, including cities and unincorporated areas adjacent to Los Angeles, these jobs would be preserved within the region, but the City would lose the resulting tax base and economic activity.

- Increase of 2,900 direct and indirect jobs coming from the annual expenditure amount for construction and support of nonprofit groups. About two-thirds of these jobs, however, would only be created as new construction begins, while the experience with Prop HHH indicates that they could be delayed by as much as 5-6 years from funds award. The job losses, however, would begin immediately.

Background

Proposed Initiative

The Los Angeles Transfer Tax contains the following provisions:

- Imposes an additional tax on the transfer of real property: 4.0% on property valued at $5 to $10 million and 5.5% on property $10 million or more. This amount would be in addition to the current 0.56% and state and local transfer taxes on properties valued at more than $100. These thresholds would be adjusted annually presumably beginning 2023 based on the US Chained Consumer Price Index.

- The tax applies to a broad range of transfers including property "*granted, assigned, transferred or otherwise conveyed to, or vested in, the purchaser or purchasers, or any other person or persons, by his or their direction.*" The Director of Finance is also empowered to further define the term "realty sold."

- The tax applies to all property except for tax exempt affordable housing organizations such as many of the measure's proponents, entities exempt from the city's taxation powers, and other affordable housing properties as later determined by the City Council. There is also an exemption in Section 21.9.15(a) written in the type of legislative language suggesting it covers a specific organization.

- Funds are to be allocated to the following purposes, with the Effective Share shown in the table below indicating the share of the tax going to the specific programs following the two-stage allocation process contained in the measure:

Initiative Share	Effective Share	Purpose
8.0%	8.0%	**Administration, including Tenant Council**
92.0%		**House LA Fund, of which:**
70.0%		**Affordable Housing Program, of which:**
22.5%	20.7%	multi-family affordable housing
22.5%	20.7%	alternative models of multi-family affordable housing
10.0%	9.2%	acquire/rehab existing affordable housing
10.0%	9.2%	homeownership assistance programs
5.0%	4.6%	program stabilization fund
30.0%		**Homelessness Prevention Program, of which:**
5.0%	4.6%	short term rent emergency assistance
10.0%	9.2%	rent burdened income support
10.0%	9.2%	eviction defense/prevention
2.0%	1.8%	tenant outreach and education
3.0%	2.8%	protections from tenant harassment
	100.0%	**Total**

- Use of any monies from this fund for low rent housing by public agencies is deemed authorized by the voters in accordance with Article XXXIV of the state Constitution, with no further voter approval required for the life of the tax.

- Any project receiving construction or rehab funds from the measure is subject to prevailing wage requirements. Projects with more than 40 units are subject to the city's project labor agreement (PLA) unless another PLA is approved. Other language, however, limits funding eligibility only to projects of 40 units or more under the multi-family affordable housing and alternative models of multi-family affordable housing program elements. As a result, all new construction of affordable housing under the measure will be subject to a PLA.

- Department of Housing can allocate up to $50 million to a project without further City Council action or approval, a threshold that likely would cover all affordable housing projects in the City since at least 2017.

- The city's Gann Limit is increased for four years by the amount of taxes collected under this measure. However, the proposed budget for 2022-23 indicates current City appropriations are $2.5 billion under the Limit for 2021-22 (34.3% of the City's Appropriations Limit), and $2.4 billion under for 2022-23 (31.9%). This provision consequently appears to needlessly expand room for yet additional tax proposals in this period.

Current Homeless Programs

Local voters previously have approved funding for homeless programs under two measures:

- City voters approved Prop HHH in 2016 to provide $1.2 billion in bond funds for construction and rehab of affordable housing.

- County voters approved Measure H in 2017 in 2017 to impose a quarter cent sales tax for 10 years to support homeless services. This tax produces about $355 million a year.

The proposed measure basically expands these existing programs within the City, by adding permanent funding for Prop HHH activities under the Affordable Housing Program component and adding the new Homelessness Prevention Program component to provide many of the same services supported by county funding under Measure H.

The state in recent years also has provided substantial funding to local governments and state agencies for affordable housing and homeless services, from both federal pandemic assistance funds and the state's recent large surpluses. Combined, the 2021 and 2022 Budget Acts allocated $11.2 billion for affordable housing and $10.2 billion for homeless programs.[1]

In addition to this surge in available housing funds, a core financing source for affordable housing continues to be the federal and state Low-Income Housing Tax Credit (LIHTC) Programs administered through the State Treasurer's California Tax Credit Allocation Committee (CTAC). As taken from the CTAC Annual Reports, funding (state and federal credits; 9% and 4% programs) to

[1] California Department of Finance, 2022-23 State Budget, Enacted Budget Summary.

projects in the City has averaged just over $100 million annually over the past 5 years. In part reflecting the higher local construction costs, Los Angeles projects have received a consistently higher proportion of total credits awarded each year when compared against the City's share of state population.

LIHTC Funding	City of Los Angeles Projects ($ mil)	Share of State Total	Population Share
2017	$49.0	15.1%	10.1%
2018	$71.1	17.6%	10.1%
2019	$76.9	16.9%	10.1%
2020	$181.7	16.6%	10.0%
2021	$133.3	11.6%	9.8%

Source: California Tax Credit Allocation Committee Annual Reports; Department of Finance Population Estimates

In addition to these sources, additional affordable housing financing and homeless program funding comes from private capital, federal grants and loans, and nonprofits.

Homeless in Los Angeles

As reported in the annual Point-in-Time surveys conducted by Los Angeles Homeless Services Authority in conjunction with US Department of Housing & Urban Development (HUD), the number of homeless in the City rose 45% between 2016 when voters approved Prop HHH to reduce homelessness, and the latest data in 2020. Overall, the City has averaged two-thirds of the total homeless in Los Angeles County in this period.

Total Homeless	City	County Total
2016	28,464	43,854
2017	33,138	42,442
2018	31,285	49,955
2019	35,550	56,257
2020	41,290	63,706

Source: Los Angeles Housing Services Agency

Due to pandemic factors, the 2021 survey in Los Angeles County addressed only the number of sheltered homeless (about 30% of the total) and did not include unsheltered individuals. The 2022 survey is complete, but the results currently are not expected to be released until September.[2]

Prop HHH Audits

Prop HHH contained a requirement for annual audits by the City Controller. To date, the Controller has issued three audits largely concentrating on the same issues related to this program: (1) the development costs per funded affordable housing unit are too high and (2) current

[2] Los Angeles Housing Services Agency, LAHSA Working With HUD to Release 2022 Homeless Count Results This Summer, press release, July 6, 2022.

procedures have significantly prolonged the development and construction process for new affordable units, taking up to six years to complete while the number of homeless keeps increasing.

The first Audit in 2019[3] concluded that the high development costs and delays in the City's program likely would cause it to fall far short of what was promised to the voters. Costs were nearly double the levels assumed in the City's initial program plan. Construction progress in opening new units was not even keeping up with the growth in the number of homeless. As a result, the program was likely to fall about a quarter short of its intended goals (later raised to about a fifth short in the 2022 Audit):

- *This review found that, regardless of the actual target, high costs and slower than expected pre-development and construction timelines have significantly hindered the City's ability to achieve the ballot measure's intentions. (cover letter)*

- *. . . more than two years after the first bond issuance and nearly three years since voters approved HHH, not one bond-funded unit has opened. While 19 projects are under construction and two are scheduled to open in the coming months, it is clear that the City's HHH program is not keeping pace with the growing demand for supportive housing and shelter. According to the Greater Los Angeles Homeless Count, homelessness in the City has increased by 40 percent to more than 36,000 people over the past four years. (cover letter)*

- *Although the number of units did not appear in the language of the ballot measure, the development of* ***10,000*** *supportive housing units through Proposition HHH is generally understood as the target and appears on the Mayor's website and City Council documents.*

  In contrast, the City's Housing and Community Investment Department (HCIDLA) . . . plan is to deliver a total of ***10,000*** *supportive housing units within ten years through separate development pipelines –* ***7,000*** *through Proposition HHH and* ***3,000*** *through non-Proposition HHH sources.*

  Assuming all of the pending projects are approved, Proposition HHH will provide 7,640 total housing units, of which 5,873 will be supportive housing. *(p. 3, emphasis in original)*

- *Building cost estimates skyrocketed from $350,000 for a small studio or one-bedroom unit and $414,000 for a larger unit, as projected in 2016, to a median cost of $531,000 per unit today. More than 1,000 HHH units are projected to exceed $600,000, with one project topping $700,000 per unit.*

  The cost of building many of these units exceeds the median sale price of a market-rate condominium in the City of Los Angeles and a single-family home in Los Angeles County. (cover letter)

The 2020 Audit[4] found that these problems continued to persist, and recommended that the City instead reconsider its entire housing program given the rising costs and growing delays embodied in the Prop HHH approach:

- ***The City should reconsider this plan.*** *The issue is not whether the City should invest in supportive housing using HHH funds – the issue is whether the City should almost exclusively pursue an approach that frequently costs more than* ***$600,000*** *per unit and takes up to* ***six*** *years to complete when there are* ***29,000*** *unsheltered Angelenos and an average of* ***three*** *lives lost every day in LA County. (pp. 9-10, emphasis in original)*

[3] Los Angeles City Controller, High Cost of Homeless Housing: Review of Proposition HHH, October 8, 2019.
[4] Los Angeles City Controller, Meeting the Moment: An Action Plan to Advance Prop. HHH, September 9, 2020.

- *Today, more than three years after the first bond issuance and nearly four years since HHH's approval, only three bond-funded supportive housing projects are open. There are 5,522 supportive units and 1,557 additional units in the pipeline, but 73 percent are not yet in construction. (cover letter)*

- *My office's 2019 audit uncovered that supportive housing projects typically take three to six years to complete from concept to occupancy. COVID-19's impact on these already lengthy timelines is not clear, but will almost certainly extend them, and it is possible that some projects in the pipeline today may never come to fruition. Before the pandemic hit, the City had already granted time extensions for 15 projects in pre-development, ranging from 42 days to more than one year, because of permitting problems, financing complexities and lawsuits. Not only do delays slow projects down, they also increase development costs. (cover letter).*

- *Not only are HHH timelines out of step with the demand for housing, rising program costs are as well. For projects in construction, the average per-unit cost increased from $521,000 in 2019 to $531,000 this year, with the highest per-unit cost reaching $739,000. And the share of units costing more than $600,000 spiked from 10.8 percent in 2019 to 28.5 percent today. Similarly, one-third of the units in pre-development will exceed $600,000, and per-unit averages increased from $507,000 to $558,000 in the past year. The highest total development cost for a single project in pre-development now surpasses $76 million. (cover letter)*

The most recent 2022 Audit[5] again concluded that the same problems were plaguing progress under the Prop HHH program, even after considering changes made in an attempt to expedite projects and taking into account additional pressures from pandemic factors. This failure was not placed on a lack of funds, but how the Prop HHH program had chosen to spend its available funds. Five years after voters approved HHH as the centerpiece of the City's homeless strategy, this audit found that only 1,142 units had been completed:

- *. . .* ***HHH is still unable to meet the demands of the homelessness crisis.*** *The cost of each unit continues to rise and the pace of development remains sluggish. (cover letter, emphasis in the original)*

- *Overall HHH per-unit costs in the primary pipeline continue to climb to staggering heights. For projects in construction, the average per-unit cost increased from $531,000 in 2020 to $596,846 in 2021.* ***Fourteen percent of the units in construction exceed $700,000 per unit, and one project in pre-development is estimated to cost almost $837,000 per unit . . .*** *(cover letter, emphasis in the original)*

- *The number of completed housing projects and projects in construction increased since our last review. But per unit costs continue to climb to excessive levels—****over $800,000 in one instance****—and the total number of completed units* ***(1,142)*** *is wholly inadequate in the context of the ongoing homelessness emergency. (p. 1, emphasis in original)*

- *The graph below provides a snapshot of actual and estimated completion dates for all housing units funded through Proposition HHH since the ballot measure was approved—****more than half of the total units are not scheduled to be completed until January 2023 or later.*** *(p. 5, emphasis in original)*

The various audits also assess the causes behind the rising costs and delays in the current program. The core identified problems include: (1) multiple loan and grant sources[6] involve separate funding application and decision processes with different timelines and different project requirements, (2) the regulatory process for these units is slow and often entails substantial additional compliance costs, (3) restricting developers to those with a record in affordable housing limits the potential construction and financing pool, and (4) higher labor costs come from the prevailing wage and PLA

[5] Los Angeles City Controller, The Problems and Progress of Prop. HHH, February 23, 2022.
[6] The 2019 Audit found the average project required 7 different funding sources.

requirements. In all, the additional requirements under the current program have increased the project "soft costs" (such as development fees, consultants, financing) to 35% to 40% of total project costs, or nearly as much as the cost required for labor and construction materials.

- *Reasons for this include the number and complexity of funding sources required to complete an HHH project, the relatively limited pool of eligible developers, regulatory barriers and permitting challenges, and considerable construction and labor costs. An unusually high 35 to 40 percent of costs are so-called "soft costs" (development fees, consultants, financing, etc.), compared to just 11 percent for actual land costs. (2019 Audit, cover letter)*

- ***Los Angeles is an expensive place to build multifamily housing—that challenge is embedded into the cost of developing supportive housing through Proposition HHH.*** *It is further complicated by a combination of cost factors including prevailing wage requirements, financing complexity, land use issues, project labor agreements, and building characteristics (e.g., enhanced accessibility standards). (2022 Audit, p. 3, emphasis in original)*

- *There are also specific factors associated with building supportive housing—both generally and in Los Angeles—that contribute to high project costs. Our previous reviews of Proposition HHH highlighted several key factors such as the overall high cost of construction in Los Angeles, prevailing wage requirements, funding complexity, regulatory issues, land use challenges, and supportive housing characteristics (e.g., enhanced accessibility standards). In addition, research by the RAND Corporation recently highlighted that project labor agreements—which are required for all HHH projects at least 65 units—can increase construction costs by approximately 15%. (2022 Audit, p. 17)*

- *The high price of development is linked with elongated approval and construction timelines. HHH projects are estimated to take between three to six years to complete — a schedule plainly out of step with the City's urgent need to bring tens of thousands of people off the streets and into housing. (2019 Audit, cover letter)*

- *The cost of land in Los Angeles is often cited as a significant cost driver for Proposition HHH housing developments, but data provided by the City's Housing and Community Investment Department (HCIDLA) shows that this point is likely overstated relative to the other categories for projects currently under construction.*

  Developers are spending approximately 40 percent of overall project costs on soft cost components such as fees, consultants, and financing. These costs are nearly as much as the cost of labor and materials to build Proposition HHH-funded housing developments. *(2019 Audit, p. 5, emphasis in original)*

- *Proposition HHH regulations require lead developers to demonstrate a history of building and managing supportive housing projects. . . this requirement can also impede competition and prevent developers from outside the traditional supportive housing community – who may bring new and innovative ideas – from participating. (2019 Audit, p. 17)*

One of the more contentious issues in the cost drivers cited in the audits is the effect of prevailing wage and PLA requirements. Proponents for this type of requirement often claim there are no meaningful cost differences. The RAND study[7] cited above specifically found four effects coming from the PLA requirement under Prop HHH:

- *The evidence strongly suggests that developers responded to the PLA by disproportionately proposing housing projects that fell below the 65-unit threshold. (p. vi)* Rather than addressing the cost effect, the proposed measure attempts to counter this outcome by reducing the PLA threshold to 40

[7] RAND Corporation, The Effects of Project Labor Agreements on the Production of Affordable Housing, Evidence from Proposition HHH, 2021.

units and then limiting funding under the two primary housing elements only to projects of 40 or more units.

- The PLA requirement had a strong effect on the size of projects funded by Prop HHH. *While projects with 50 to 64 units make up more than 45 percent of the HHH sample, such projects make up less than 10 percent of the non-HHH sample. Meanwhile, relative to the corresponding HHH shares, the share of non-HHH projects with between 65 to 79 units is around 100 percent larger and the share with between 80 and 94 units is approximately 250 percent larger. (p. vii)*

- *. . . per unit construction costs were approximately $43,000 higher for projects covered by the PLA. This amounts to a 14.5-percent increase in construction costs. (p. viii)*

- *. . . in the absence of the HHH PLA, a combination of developers building larger projects and lower costs facilitating the funding of more projects would have resulted in approximately 800 more units of housing, or an amount representing around 11 percent of the total of 7,305 housing units in the actual HHH pipeline today.*

In addition, the LIHTC program regulations[8] specifically account for a substantial cost increase associated with the use of these provisions. Section 10327(c)(5)(A) of the regulations accommodates these higher costs through an increase in the allowable development cost limit used as a cutoff point for eligible projects:

- By 20% for projects "*. . . subject to a legal requirement for the payment of state or federal prevailing wages or financed in part by a labor-affiliated organization that requires the employment of construction workers who are paid at least state or federal prevailing wages.*"

- By another 5% for projects "*. . . subject to a project labor agreement . . . that requires the employment of construction workers who are paid at least state or federal prevailing wages or that they will use a skilled and trained workforce . . . to perform all onsite work within an apprenticeable occupation in the building and construction trades.*"

These costs are not just due to the wage differential. As noted in a study by UC Berkeley's Terner Center,[9] there are substantial additional costs as well coming from the extensive compliance procedures associated with these provisions, frequent delays in developers and contractors receiving authorized payments due to the additional bureaucratic reviews, cost of non-wage provisions in PLAs, and reduction in the pool of available labor and subcontractors. While these costs add up even under normal circumstances, their significance is amplified in the current construction labor shortage environment.

Rather than contain changes addressing the previous audit issues, the housing components in the proposed measure build on the Prop HHH program model, adding new permanent funding but not incorporating reforms that would reduce unit costs or the current, lengthy project approval procedures. In many instances, the additional requirements under this measure are likely to make

[8] California Code of Regulations, Title 4, Division 17, Chapter 1, California Tax Allocation Committee Regulations Implementing the Federal and State Low Income Housing Tax Credit Laws.
[9] Terner Center, The Costs of Affordable Housing Production: Insights from California's 9% Low-Income Housing Tax Credit Program, 2020.

these problems worse. These include broadening the PLA requirement coverage and continuing to restrict project eligibility to the same limited pool of developers who have struggled with timely development performance under the current Prop HHH funding levels.

The one major change in the project timeline contained in the proposed measure is to delegate more project decisions to the Housing Department, in essence all of them given the high threshold ($50 million) for this shift. This change would bypass current project approvals under Prop HHH now required by the city council and the mayor, and contains no provisions for public and expert review comparable to what is now being performed in project application reviews by the Prop HHH Citizens Oversight Committee and Administrative Oversight Committee. The measure instead replaces these bodies with a new Oversight Committee and a Tenants Council with authorities to review expenditures and activities at a program level rather than on a project application basis.

Of all the current administrative processes contributing to the 3-6 year approval delay for new affordable housing, the measure chose to make changes that reduce public oversight and public accountability for the expenditure of taxpayer funds rather than changes that would substantially shorten the current unacceptable delays. Rather than creating the "strongest oversight in LA's history" as claimed on the proponents' website,[10] this provision would replace a highly transparent public process for the selection of funded projects with a far more opaque one delegated to the City's bureaucracy.

Looking at a somewhat broader range of affordable housing projects than just those receiving Prop HHH funding, overall per unit costs in the City spiked 89% between 2016 and the most recent data in 2021. Based on data from the annual reports of the State Treasurer, California Tax Credit Allocation Committee (CTAC; both 9% and 4% programs), the per unit cost for affordable housing projects in the City of Los Angeles ranged from $497,000 to $834,000 in 2021, and averaged $630,000. Note in the table below, the surge in units in 2020 was largely the result of federal pandemic assistance allocated by the state, in particular Project Homekey which focused on lower cost renovations of motels, hotels, and other commercial properties for this purpose.

City of Los Angeles	Low Income Units	Per Unit Max	Per Unit Min	Per Unit Average	% Change
2016	2,552	$630,000	$214,000	$333,000	
2017	1,126	$599,000	$209,000	$418,000	25.5%
2018	2,076	$691,000	$232,000	$446,000	6.7%
2019	2,513	$753,000	$158,000	$478,000	7.2%
2020	4,613	$885,000	$289,000	$523,000	9.4%
2021	882	$834,000	$497,000	$630,000	20.5%

Source: Calculations from California Tax Credit Allocation Committee Annual Reports

There are other models that have proven to be far more successful in building truly affordable housing by eschewing the public programs, their added costs, and additional regulatory complications. SoLa Impact LLC currently builds low-income housing in the South Central LA area for about $250,000 a unit using only private money (including investments by CalSTRS),[11] compared to the Prop HHH current average of $600,000 and ranging up to $837,000 a unit. Projects are designed specifically to keep rents affordable in line with HUD Section 8 housing vouchers.

[10] https://unitedtohousela.com/, accessed August 1, 2022.
[11] Is the Key to the Affordable Housing Crisis More Capitalism:, Bloomberg, July 20, 2022.

Impacts from the Proposed Tax

$860 Million Annual Tax Increase

Based on an analysis of City of Los Angeles parcel data in the period 2017-2020, the proposed tax had it been in effect would have raised taxes by $740 million to $930 million (2022 dollars), or an average of $860 million a year. This range is generally consistent with but somewhat higher than the $800 million figure estimated by the initiative proponents based on one year of property sales.[12] It also is consistent with the range of $600 million to $1.1 billion annually estimated in the City's resolution.[13]

This estimate was developed through the following steps:

- All data was taken from the County Assessor parcel file.
- Parcels sold or otherwise transferred were identified as those with the current year showing for both the land base year and improvements base year.
- Total value (land and improvements) was filtered after adjusting the $5 million and $10 million thresholds in 2022 using the Chained Consumer Price Index, consistent with the proposed initiative. Only taxable parcels were included.
- The tax results from each year were then adjusted to constant 2022 dollars, again using the Chained Consumer Price Index.

To put the size of this tax increase in context, current revenue numbers for the City of Los Angeles were taken from the 2022-23 budget documents.[14] Compared to the current revenue projections, the proposed tax would represent:

- 7.9% increase in total receipts (general and special).
- 14.0% increase in taxes levied by the City.
- 27.3% increase in local property taxes. In order to provide a conservative number, this comparison considers all taxes currently imposed on property, including general property tax, property levy for general obligation bond service, parcel taxes, parcel assessments, and the current transfer tax.

Of the three comparison bases, the third is the most relevant from a policy perspective. Since voters overwhelmingly approved Proposition 13 in 1978, various interest groups have proposed a number

[12] United to House LA, United to House L.A. Citizens Initiative, Quick Summary, undated.
[13] Los Angeles City Clerk, Ballot Measures, 2022 General Municipal Election, Council File #22-1100-s2.
[14] City of Los Angeles, FY 22-23, Budget Summary.

of changes that would reverse these constitutional property tax protections either in whole or in part. Especially with the most recent failure along these lines—voters' rejection of the Proposition 15 Split Roll in 2020—these efforts have instead turned to other proposed work arounds including parcel taxes with differential charges using square footage as a property value proxy and the current proposal using the transfer tax as a capital tax based on value.

However, viewed from any of the three perspectives shown above, the proposed measure would impose the largest tax increase in the City's history. Only one existing tax source—the general property tax—would produce more revenues if this measure passes. Considering all general and specific revenue sources, only two would be larger—general property tax and the sewer construction and maintenance fund.

Only Half of Tax Proceeds Would Go to Housing

Regrouping the measure's program elements into programmatic categories, only half of the tax proceeds would go to construction and rehabilitation of housing. Just under a quarter would go to income assistance and subsidies. The remainder would be split roughly between the administrative categories and to for grants to nonprofits—such as those listed as supporters of the measure—to provide social program and legal services.

Effective Share	Purpose	$ million
50.6%	Affordable Housing Construction/Rehab	$430
23.0%	Income/Housing Assistance	200
13.8%	Other Social Services	120
12.6%	Administration & Reserves	110
100.0%	Total	$860

As discussed earlier, the average cost for an affordable housing unit in Los Angeles in 2021 from the CTAC data was $630,000. Adjusting this amount to 2022 dollars, the estimated $430 million annually for housing would be sufficient to build another net 640 units a year.

While the actual number or units supported by the tax proceeds could be higher if these funds were used to leverage other financing, the 640-unit level represents the net increase that would come as a result of the new tax.

Current publicly financed affordable housing relies on a defined set of funding sources, largely state, federal, and foundation grants and loans, tax credits, and a range of mitigation funds coming from market rate developments. Although now experiencing an upsurge due to the federal pandemic assistance funds and the state surplus, these sources have been limited—the main driver behind the current effort by the nonprofit developers and other supporters of this measure to develop a new funding source through a new tax. What leveraging that will be possible likely will still come from the same funding pool. If the leveraging opportunities were more robust, the new tax would not be needed.

Leveraging opportunities are also speculative given that the local affordable housing capacity has already demonstrated challenges in timely performance under the Prop HHH funding levels. Restrictions from that measure that limited the developer, labor, and financing base are repeated and in some cases intensified in the new measure. The SoLa Impact LLC example cited earlier indicates there is readily available private capital when affordable housing is built giving financial performance proper consideration. The proposed measure, however, is just as likely to fill in gaps caused by the soaring unit cost of publicly financed affordable housing as it will produce new supply.

Consequently, to the extent that more than 640 units are supported in part through this new tax, the other funding amounts are just as likely to have gone to Los Angeles projects regardless or, if not, are likely to result from shifting the available pool of loans, grants, and credits to Los Angeles from projects in other areas. The net 640 unit figure is the proper base of analysis for this portion of likely benefits coming from the tax. The net 640 unit figure is also appropriate given the measure's double downing on many of the cost drivers that have limited the potential from the Prop HHH funds in the first place.

It is also important to note that the 640 units represents the amount of net new housing that can be financed each year. The measure contains no provisions to speed up the abysmally slow pace of completing new affordable housing as shown in the Prop HHH results to date, and in fact likely introduces new delays through its various provisions. Rather than new housing, the net additional 640 units each year will likely serve more to increase the current project backlog.

In the most recent estimates from Department of Finance,[15] there are 1,526,672 housing units in the City of Los Angeles as of 2022, of which 100,071 (6.6%) were estimated to be vacant. From this base, the net additional 640 units would increase total housing stock in the City by 0.04% a year, or at a level that would have an insignificant effect on overall supply and rents.

Using the Department of Finance estimate of 2.6 persons per household in Los Angeles, the additional 640 units would provide housing for about 1,700 persons each year when those units finally get built. This level would cover only 4% of the 41,290 homeless individuals identified in the 2020 surveys, or at a level that would not even maintain pace with the annual increase in the number of homeless.

Two-thirds of the Tax Would Fall on Rental & Business Properties

The proponent's website[16] contains a number of incorrect statements concerning what type of properties would be subject to the new tax. These include: (1) stating that the proposal is a "tiny tax on mega mansions," (2) claiming that "Only Millionaires & Billionaires Pay," and (3) "Protects renters from . . . rent hikes."

The actual incidence of the proposed tax was evaluated again using the County Assessor parcel file data. In addition to the procedures as above, tax estimates were broken down by property type as listed in the file.

As shown in the results, "mega mansions" or single family residences (SFR) on average would pay only 28% of the proposed tax. Rental properties (MFR—multi-family residences) would pay 25%. Business properties (commercial, industrial, institutional, recreational, and agricultural) would pay

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[15] Department of Finance, E-5 Population and Housing Estimates.
[16] https://unitedtohousela.com/, accessed August 1, 2022.

the highest share at 43%. Another 4% would be paid by properties where the file designates the property type as "missing" or "miscellaneous."

While owners of these properties would be the initial payers of the tax, the two-thirds of the tax paid on multi-family and many if not all of the business properties would be passed on to household and business renters in the form of higher rents. Renters consequently would not be "protected" from this aspect of the measure and instead are likely to see their costs go higher. And while there may be some millionaires among this group, the ultimate cost impact will be on a much broader range of incomes than stated by the supporters.

Los Angeles Transfer Tax (million 2022 dollars)		SFR	MFR	Business	Misc/Unkn	Total
2017	$5-10 million	$104	$45	$45	$1	$194
	$10+ million	159	155	396	28	737
	Total	$263	$200	$441	$28	$932
	Percent	28.2%	21.5%	47.3%	3.0%	100.0%
2018	$5-10 million	$109	$52	$51	$1	$212
	$10+ million	143	126	211	44	524
	Total	$252	$178	$262	$44	$736
	Percent	34.2%	24.2%	35.6%	6.0%	100.0%
2019	$5-10 million	$106	$49	$61	$1	$217
	$10+ million	100	193	386	13	692
	Total	$205	$242	$447	$14	$908
	Percent	22.6%	26.7%	49.2%	1.5%	100.0%
2020	$5-10 million	$94	$46	$56	$1	$197
	$10+ million	155	192	270	39	656
	Total	$249	$238	$326	$40	$853
	Percent	29.2%	27.9%	38.2%	4.7%	100.0%
Average		**28%**	**25%**	**43%**	**4%**	**100%**

Source: See text

Effect on Housing Costs in Los Angeles

The measure is likely to have less of an effect on overall single-family residence prices as the thresholds keep the price increases within a discrete, higher end portion of the market. There will be effects at the margin on properties valued at less than $5 million and for all homes over this price level, but the number of properties affected will be relatively small compared to the total supply. Previous studies of similar transfer taxes[17] focused on "mega mansions," however, indicate a much wider spread of effects impacting both prices and turnover both above and below the tax thresholds, with possible implications to the longer-term potential receipts coming from the proposed tax.

[17] For example: Wojciech Kopczuk and David Munroe, Mansion Tax: The Effect of Transfer Taxes on the Residential Real Estate Market, American Economic Journal: Economic Policy 2015, pp. 214-257/

There will be a more significant effect on multi-family rentals and on commercial and other business properties—and consequently rents—as the thresholds will capture a much larger share of these properties and will not be limited to a discrete portion of the market.

Previous studies of residential property transfer taxes[18] indicate these charges are quickly capitalized into property values in instances where the tax has been generally applied and over a more uniform geographic area. In these cases, home prices in the short term fell by an amount roughly equal to the cost of the tax. However, there was also a substantial demand drop accounting for at least a portion of this price effect, with significant drops in home sales including as the result of homeowners shifting to renovations rather than purchases due to the higher transaction costs.

In the papers that broke the analysis out by price level, the effect on prices was more significant for areas with home prices below the regional median. The price effect in higher value areas was substantially less to negligible.

The Mahdi-Pinto paper looked at a more restricted application of a transfer tax, still residential but applying only to foreign purchasers in the Greater Vancouver Region. Their results also identified a decline in home prices following imposition of the tax, but accounting for only half of the tax amount. The remaining half had the effect of raising the effective price of properties subject to the tax. This paper, however, does not separate out the price effect on properties subject to the tax specifically, and instead measured changes in sales and prices more generally that resulted from a tax designed to dampen demand from a specific portion of the market.

In the case of commercial properties, another study[19] found only a portion of a transfer tax is capitalized into property values. For every rise of 1% of the tax, the study found prices fell by only up to 0.22% for offices and up to 0.19% for other commercial properties, with the remaining portion of the tax representing an increase in effective prices. Sales fell by roughly the same amounts, again indicating a demand effect on the price rather than one driven purely by the tax cost. Cross-border effects, however, were more significant. A 1% increase in the tax by a neighboring state led to a 0.51% increase in prices for other commercial properties, indicating a likely shift in investments from the state with a tax increase.

The relevance to the proposed Los Angeles tax from these studies is mixed. Applied only to higher value properties, the tax is more akin to the Vancouver experience. The commercial results from the Baudisch-Dresselhaus study, however, suggest the primary effect of the tax will be to raise the property transaction costs for these properties and eventually prices as they rise to incorporate these additional costs. Los Angeles—not just neighbored by areas without such a tax but surrounded and

[18] For example: John D. Benjamin, N. Edward Coulson & Shiawee X. Yang, Real Estate Transfer Taxes and Property Values: The Philadelphia Story, The Journal of Real Estate Finance and Economics, September 1993, pp. 151-157; Benjamin Dachis, Stuck in Place: The Effect of Land Transfer Taxes on Housing Transactions, C.D. Howe Institute, Commentary No. 364, October 2012; Ben Dachis, Gilles Duranton and Matthew A. Turner, The Effects of Land Transfer Taxes on Real Estate Markets: Evidence From a Natural Experiment in Toronto, Journal of Economic Geography, 2012; Hamza Mhadi and Jairo Pinto, Assessing the Effects of the Vancouver Foreign-Buyer Transfer Tax on Housing Prices and Volume, Western Undergraduate Economics Review Annual 2018, June 2018.

[19] Coletta Frenzel Baudisch and Carolin Dresselhaus, Impact of the German Real Estate Transfer Tax on the Commercial Real Estate Market, Justus-Liebig-Universität Gießen, Finanzwissenschaftliche Arbeitspapiere Nr. 100 – 2018, December 2018,

interlaced with them—is likely to see any short term price effects from the tax countered as price pressure shifts to the broader region.

Using a simplified analysis, the top tax rate of 5.5% would lead to upward pressure on residential and commercial/industrial rents by the following amounts:

- Up to a 5.5% increase if evaluated based on the increase that would be needed to produce equivalent cap rates for the properties subject to the tax.

- Up to an 8% increase if evaluated at what increase would be required to produce an equivalent after tax rate of return.

This analysis is based on the following factors and assumptions: (1) current commercial loan rate of 4.6%, at the weighted average based on the parcel distribution from the sales analysis above and 75% for commercial/industrial and 80% for multi-family residential, (2) current federal and state corporate tax rates (although properties are more likely to be held by an LLC or partnership taxed on a pass-through basis), (3) average Los Angeles property tax rate, and (4) straight-line depreciation over 27.5 years.

Employment Effects

The annual increase in taxes by $860 million (2022 dollars) would result in the loss of 4,000 direct and indirect jobs in Los Angeles County, as well as a likely shift of jobs away from the City that could affect up to another 33,100 direct and indirect jobs as the additional tax costs affect the economics of local investments. These losses would be offset to some degree by an increase of 2,900 direct and indirect jobs resulting from expenditure of the tax receipts, but these would be limited by the high development costs of any units that would be produced under this measure and the high share of the tax receipts that would go to transfer payments.

Employment effects were estimated using the 2020 RIMS II input-output multipliers (Type I) obtained from US Bureau of Economic Analysis for Los Angeles County. All inputs consequently were adjusted to 2020 dollars.

The direct and indirect employment effects of 4,000 jobs was calculated based on the portion of the new tax paid by business operations, as shown in the previous table, consisting of $370 million paid by the business portion and $215 million paid by multi-family rentals. The portion attributable to miscellaneous/unknown was not included. The business portion was estimated using a weighted average of the affected industries.

Additional job impacts would come as the tax undermines the economics of capital investment in the city both through the higher transaction costs and by putting upward pressure on property values, especially as compared to investment opportunities elsewhere in the county and region. Projects otherwise slated for the City consequently would be passed over for funding in favor of investments elsewhere in the region and the US. Potential investments in the City consequently would be reduced, delayed, or shifted to more cost-effective locations in the county and region.

Existing construction (new, rehabilitation, additions) in the city that could be affected by the tax threshold levels was estimated by again using the County Assessor parcel data. The period 2018-2020 shows an average of up to $3.6 billion annually for commercial, industrial, institutional, and other business improvements, and $1.8 billion in multi-family residential (2022 dollars). The numbers cover properties with a total valuation of $4 million (2022 dollars) or more to account for those most likely to be immediately affected by valuation changes as the result of the new tax. The values shown cover only improvement values (construction values) and do not include land costs.

Using the annual average improvement values from the Assessor parcel file, the tax would affect annual investments providing up to 33,100 direct and indirect jobs within Los Angeles County. Not all of these jobs would be eliminated. Some projects could still move forward but at higher costs that would affect overall project economics and scale. To the extent that investments move to other locations in the county, including cities and unincorporated areas adjacent to Los Angeles, these jobs would be preserved within the region, but the City would lose the resulting tax base and economic activity.

Expenditure of the tax revenues would generate some offsetting jobs. To calculate these, the portion allocated to housing construction was adjusted to remove land costs based on data in the annual audits. The improvements portion was then adjusted for prevailing wage and PLA effects using the results of the Terner study (prevailing wage) and CTAC credit amount (PLA) to use a more conservative estimate rather than the higher levels from the RAND study and CTAC credit for prevailing wage. No adjustments were made for the other higher cost factors identified in the annual audits, but incorporating these would lower the overall job results. After making these adjustments, offsetting direct and indirect jobs coming from the annual expenditure amount for construction and support of nonprofit groups would total 2,900.

About two-thirds of these jobs, however, would only be created as new construction begins, while the experience with Prop HHH indicates that they could be delayed by as much as 5-6 years from funds award. The job losses, however, would begin immediately.

Additional impacts are possible. As noted above, previous research on the effects of transfer taxes has been consistent in finding a slowdown in property sales as the taxes are first imposed. Given the geographic pattern in which the City of Los Angeles exists, this outcome is likely to see a shift in property sales and investment activity to neighboring cities and other counties in Southern California for both residential and, as discussed above, business properties. This outcome would affect the potential annual receipts from the new tax, and add another source of volatility to what will already be a revenue stream that is already likely to vary widely year to year in response to factors such as the economy, the economic health of key local industries, and quality of life factors affecting both the level of sales and property values.