Harry Kim
Mayor

Christopher J. Yuen
Director

Brad Kurokawa, ASLA
LEED® AP
Deputy Director

County of Hawaii
PLANNING DEPARTMENT
101 Pauahi Street, Suite 3 • Hilo, Hawaii 96720-4224
(808) 961-8288 • FAX (808) 961-8742

RECEIVED
2008 SEP 10 AM 9 00
COUNTY CLERK
COUNTY OF HAWAII

September 9, 2008

Honorable Pete Hoffmann
Chair and Presiding Officer
and Members of the County Council
COUNTY COUNCIL
333 Kilauea Avenue, Second Floor
Hilo, HI 96720

Dear Chair Hoffmann and Members of the County Council:

SUBJECT: BILL 324 – IMPACT FEES

Bill 324, to create a new Chap. 36, establishing impact fees in Hawai'i County, is currently pending before the Council. This is one of the most important legislative decisions the County has considered in recent years. This memo tries to summarize the pros and cons of adopting impact fees.

Basic Principles

An impact fee is a fee charged on new development to fund infrastructure and public facility demands that will be generated by that development. People moving into new homes will use public parks, highways, fire stations, and other facilities. Impact fees are a one-time charge to create a fund to build new facilities to meet that demand. They are generally imposed when a building permit is issued, although the draft bill allows them to be imposed at final subdivision approval for residential subdivisions.

Impact fees must be assessed and administered according to a state law, H.R.S. sec. 46-141 to 148. The law requires a needs assessment study that identifies the kinds of facilities that the fee would pay for. The study also determines the maximum amount of impact fee that can be charged for these facilities. It is based on the cost to duplicate the current facilities that the county has, to accommodate the new development.

Comm. No. 1329.14
Ref. To: PC
Ref. Date SEP 10 2008

Hawai'i County has completed the necessary study, the "Infrastructure and Public Facilities Needs Assessment: Impact Fee Study" September 2006, prepared for the Planning Department by Duncan Associates with Helbert Hastert & Fee. This establishes maximum fee levels for roads, parks, fire/EMS, police, solid waste and wastewater (sewer.) Water was not included because the Department of Water Supply, which is the only body authorized to impose impact fees for water, has a fee schedule for water commitments.

In the draft bill, the impact fee is proposed to be 50% of the maximum amount established in the study. The county could impose any percentage up to the maximum. Sec. 36-12 of Bill 324 includes a table showing these proposed fees. For example, the fee for a single-family home would be $6,387.00 (not counting any sewer fee), and $4.97 per square foot for a retail/commercial project. The fees are broken down into different categories of public facilities. Roads and parks make up about 90% of the total impact fee for houses. The fees for police, fire, and solid waste facilities are relatively small.

Impact fees can be used only for facilities that are needed to accommodate new development—that is, they need to be capacity-enhancing projects. For example, the county can build a new gym with impact fees, but it cannot repair the roof on an old gym. It can add lanes to an existing road with impact fees, but cannot use them to resurface an existing road. Projects funded with the fees must also be spent in the area that generated the impact fees, which are called "benefit districts," but the County has some flexibility in defining the benefit districts.

New development that is required by its rezoning ordinance or other land use approval to build infrastructure that meets regional needs—such as a major road or park—will be entitled to offset the value of such improvements against the impact fee for that category. For example, Parker Ranch would offset the value of the connector road and its park land dedications required in its rezoning ordinance, and Hokuli'a would offset the value of the Mamalahoa Bypass and some park contributions.

The impact fee would replace the "fair share" condition that has been placed on most residential and resort rezoning in Hawai'i County since the early 1990's. The impact fee is much broader than fair share because it would apply to all new development, not just projects that were rezoned. So, for example, it would apply to new homes built on lots in subdivisions created in the 1950's and 1960's. It also applies to a broader range of development than fair share, such as retail and industrial buildings, churches, and private schools.

Impact fees are a revenue-generating tool. As such, they must be evaluated against other options, such as property taxes, the fuel tax, and funding mechanisms that are specific to a development project, like community facilities districts.

Pros

1. Impact fees will generate substantial revenues.

The amount of revenue depends upon the amount of development. Home construction on the island varies greatly, in cycles usually following nationwide economic trends. In 2005, the high point of the current cycle, we had building permits issued for 3,501 new single-and multi-family units. In 2007, there were 2,168 units, and, if the pace for the first seven months of 2008 continues, we will have only about 1,200 building permits for new dwelling units issued this year. The long-term average for the 1980-2007 period is about 1800/yr. From this figure, we must deduct the homes in projects that will have offsets due to zoning requirements, and the affordable housing grants discussed below. If we assume that impact fees will be paid on 1,500 residential units per year, and that 80% are single-family, at $6,387/unit, and 20% are multi-family (this is close to the historical average), at $4,734/unit, impact fees on new residential construction would generate about $9 million/yr.

The amount from nonresidential development is very hard to estimate because we would have to do an analysis of the annual square footage of different types of buildings, but it is certainly much less than the residential. $2 million/yr. is a reasonable estimate, based on building permits taken out in recent years.

Of this estimate of about $11 million/yr., about 40% would go to roads, about 50% to parks, and police, fire, and solid waste would cumulatively be about 10%. These percentages are approximate because of offsets and the fact that there are different fee levels for different types of development.

Revenues of $11 million/yr. would cover the annual interest and principal payments on a $133 million bond at 5% interest and a 20 year term. In practice, because annual impact fee revenues will vary greatly, we could not count on impact fees being the sole source of funding for a bond of this magnitude, but this gives an example of the funding potential.

In comparison, annual real property tax revenues for the 2008-2009 fiscal year are projected at $232 million. If impact fees were $11 million/yr., they would equal about 5% of real property tax revenues. Or, to put it another way, it would take a 5% across-the-board increase in real property tax rates to yield this level of impact fee revenues.

This analysis assumes that impact fees do not significantly reduce the level of development. At the fee levels proposed in Bill 324, this seems a reasonable assumption.

2. Impact fees have a sound legal basis.

Questions have been raised about the legality of the "fair share" assessment system. Although there was a study to establish the level of assessments in the early 1990's, the system was never enacted by a comprehensive ordinance. Although there are legal defenses of this practice, and it has never been directly challenged by someone liable for fair share payments, the impact fee has a more solid legal basis.

It should be noted that even if the courts ultimately invalidated "fair share" assessments, the specific improvements required by many of the rezoning ordinances, such as road construction or the dedication of land for parks, would still be valid because they are rationally related to the impact of those projects. In practice, many projects, especially the larger ones, have not paid fair share for roads or parks because they are building roads or dedicating parks which qualify for an offset.

3. Impact fees provide funds for new infrastructure in areas experiencing rapid growth.

The development of new county facilities has not matched the trends in population growth. Since 1970, most population growth in the island has occurred in Puna (about 35% of the island's population growth), North Kona (about 26% of the island's population growth), and South Kohala (about 14% of the growth). At the same time, the proportion of the island's population living in the South Hilo district has dropped from 53% to less than 30%. The overall population of the Big Island has almost tripled since 1970.

Development of county facilities has not kept up to serve the fast-growing areas of the island. There are many reasons. For example, if the roof of an old gym leaks, and is going to rot the floor, fixing the roof is going to be a budget priority. But a series of decisions like this tends to reinforce investment in existing facilities that serve the older population pattern, rather than spending money where the population has moved. Impact fees must be spent on facilities that increase capacity, such as new parks or new roads, and must be spent, at least generally, to benefit the regions where the fees are collected, so this will tend to follow the growth in population.

4. Impact fees tend to make new developments pay for the new infrastructure.

Impact fees are charged to new development, which is creating the need for new parks, roads, and other county facilities. In that respect, it may seem fairer to charge those buying into those developments for new facilities.

5. Impact fees will generate substantial funds from areas where zoning conditions don't require developers to provide improvements.

At least 50% the new homes in the island are being built in the subdivisions created from the 1950's to 1970's like Hawaiian Paradise Park and Hawaiian Ocean View Estates. In some years, 60-70% of new homes may be built on lots subdivided before 1980. In these areas, no zoning conditions require developers to provide parks or other improvements. Impact fees will generate major revenues which can be used to build facilities for these areas, especially parks. (This is the flip side of one of the "Cons" discussed below—that individual lot owners will have to pay impact fees.)

Cons

1. Impact fees may increase costs to home buyers.

Obviously, someone pays the impact fee. It is not so obvious who ultimately bears the cost. When a developer builds homes, even though the developer actually pays the fees when getting the building permits, it is not clear whether the developer bears the cost in the end, accepting a lower profit. It is possible that the developer passes the cost on to the home buyer, or that the developer will offer less when buying land on which to build a project. If you think of the homebuilding process as involving three main players: (1)

the owner of the raw land, who sells it to (2) the developer, who builds the homes, and sells them to (3) the home purchaser, the impact fee can conceivably be absorbed by any of these three, or by a combination of all three.

This issue has been studied extensively on the Mainland, without a firm conclusion, and perhaps the fairest thing that can be said is that it may depend upon market conditions.

Given the affordable housing problem on the island, we do not want to push the cost of housing higher, and given the scarcity of developers doing affordable housing, we would also not want to discourage them by decreasing their profit potential.

Bill 324 contains a number of provisions designed to lessen the effect on affordable housing, in sec. 36-10. In summary, the County would pay the impact fee for designated affordable housing or offer loans to cover the impact fee. For legal reasons, the County should not just "waive" the impact fee. The affordable housing grants and loans will require considerable administration and recordkeeping.

If the impact fee is ultimately passed on to the home buyer, it then becomes part of the purchase price and typically is financed within the mortgage. At a 6.25% mortgage, over 30 years, a $6,387 impact fee would cost the buyer about $38/mo.

2. Individual owners of lots would have to pay impact fees.

Individuals who currently own lots and want to build homes on them obviously will bear the impact fee themselves. They cannot pass it on to someone else. This is clearly a large group of local residents, even though an analysis done with the impact fee study shows that only about 30% of vacant lots are entirely or partially owned by a Big Island resident. Some lot owners may get relief from the affordable housing provisions of Bill 324, but many will not. Again, although the one-time charge is high, if the owner is financing the home, the monthly amount, rolled into a mortgage, is modest.

3. Impact fees may have a bigger negative effect on lower cost housing than raising a similar amount from property taxes.

Assuming that impact fees are ultimately carried by the home purchaser (see the discussion above), they have a bigger effect, proportionally, on lower priced housing because they are flat fees. Legally, the impact fee can be varied slightly based on the size of the house, but the difference is small: only about 30% more for a 4,000 square foot house vs. a 1,000 square foot house. For simplicity's sake, Bill 324 did not vary the fees by house size.

In contrast, property taxes are proportionate to value. For example, the property tax bill for a home with a taxable value of $100,000, after applying all exemptions, in the homeowners' class, is $555/yr., whereas for a home with a taxable value of $1,000,000, after exemptions, the property tax bill is $5,550/yr. A 5% across-the-board increase in property tax rates (to generate the equivalent of an impact fee) would cost the owner of the $100,000 home $27.75/yr., while the owner of the $1,000,000 home would pay an additional $277.50/yr.

In this sense, impact fees can be considered regressive compared to property taxes, again, if the homebuyer bears the cost of the impact fee.

4. The County will have to budget operating funds for the new facilities, especially parks.

If the County builds new parks with impact fees, it also has to budget funds to operate the parks from other revenue sources. By law, impact fees cannot be used for operating expenses or salaries. The operating and maintenance costs for roads are relatively low compared to the capital costs, and the impact fee will not generate enough funds to greatly increase county investment in police, fire, or solid waste facilities.

5. Impact fees involve considerable administrative costs.

Naturally, these fees have to be collected and put in the proper accounts. The interface with the fair share system creates some administrative issues (the prior fair share payment has to be offset against any impact fee.) The affordable housing grants and loans will also require much record-keeping and administration to determine eligibility. The impact fee program will need additional staff in Planning, Finance, DPW-Building Division, and the Office of Housing and Community Development.

6. The proposed impact fees are less than the "fair share" assessments.

The current "fair share" assessment is about $11,500 for a single-family dwelling.

Because Bill 324 sets the impact fee at 50% of the maximum, it is only $6,387, so some developments which have "fair share" conditions will pay less if Bill 324 is adopted than under their current requirements. This is not the case, however, for those developments that are building roads and dedicating park land in excess of the "fair share", because they would offset the fair share in any case.

7. The County may not have road projects planned to benefit some areas.

Impact fees for roads should be spent on major collector or arterial roads that are used by a large number of people, not on roads with a strictly local function. In Puna and Ka'u, the major roads used by most residents are state highways. The impact fee law allows the counties to give their impact fees to the state for highway projects, but we have little control over the timing and implementation of state projects. In Puna, the county is considering a Puna Makai Alternate Route ("PMAR") as a county project, but this is in the planning stages. In Ka'u, about 75% of the new homes have been built in the Hawaiian Ocean View Estates area, and there are no County road projects planned in Ka'u which really serve HOVE.

More Information

More relevant information is contained in "Infrastructure and Public Facilities Needs Assessment: Impact Fee Study" September 2006, prepared for the Planning Department by Duncan Associates in association with Helbert Hastert & Fee. This study and other related information on impact fees are posted on the Planning Department website—www.co.hawaii.hi.us/planning/ipfna. Also, the Duncan Associates website, ImpactFees.com, is a great source of information about impact fees.

Sincerely,

CHRISTOPHER J. YUEN
Planning Director

CJY:pak
Wpwin60/Chris 08 – Hoffmann –Bill 324 - Impact Fee Summary