



OFFICE OF THE CITY AUDITOR

City and County of Honolulu
State of Hawai'i



Audit of the City's Management of Unilateral Agreements in Affordable Housing

A Report to the
Mayor
and the
City Council of
Honolulu

Report No. 07-05
October 2007

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Submitted by

THE CITY AUDITOR
CITY AND COUNTY
OF HONOLULU
STATE OF HAWAII

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Foreword

This audit was conducted pursuant to Resolution 05-285, CD1, *Requesting the City Auditor to Audit the City's Affordable Housing Program*, which was adopted by the Honolulu City Council on October 19, 2005. The resolution requested the city auditor to review and assess the city's use of affordable housing conditions in unilateral agreements, the adequacy of current staff to monitor, administer, and enforce affordable housing conditions in unilateral agreements, and the appropriateness of the selling prices of affordable housing units developed under unilateral agreements. During our preliminary review, we found that some of the issues identified in the resolution were recently addressed by other government and industry groups. Rather than re-examine these issues, and due to limited resources, we chose to focus this audit on the city's administration of in-lieu fees and application of excess affordable housing credits, as they directly affect the number of affordable housing units *actually* built.

We wish to express our appreciation for the cooperation and assistance provided to us by the staff of the Department of Planning and Permitting, Department of Budget and Fiscal Services, and others who we contacted during this audit.

Leslie I. Tanaka, CPA
City Auditor

EXECUTIVE SUMMARY

Audit of the City's Management of Unilateral Agreements in Affordable Housing

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This audit was conducted pursuant to Resolution 05-285, CD1, *Requesting the City Auditor to Audit the City's Affordable Housing Program*, which was adopted by the Honolulu City Council on October 19, 2005. The resolution requested the city auditor to review and assess the city's use of affordable housing conditions in unilateral agreements, the adequacy of current staffing to monitor, administer, and enforce affordable housing conditions in unilateral agreements, and the appropriateness of the selling prices of affordable housing units developed under unilateral agreements. During our preliminary review, we found that some of the issues identified in the resolution had been addressed by other government and industry groups in recent years. Rather than re-examine these issues, and due to limited resources, we chose to focus this audit on the city's administration of in-lieu fees and application of excess affordable housing credits as they directly affect the number of affordable housing units *actually* built.

Background

During the 1970s local governments across the country began implementing "inclusionary zoning" or "inclusionary housing," which required developers to set-aside a certain percentage of housing units for low- and moderate-income households within otherwise market-rate developments. At the same time, the City and County of Honolulu began imposing various requirements on land use rezoning to ensure the production of affordable housing through "unilateral agreements" by ordinance. The city estimates that nearly 13,000 affordable housing units have been constructed for sale or rent under the affordable housing requirements imposed by unilateral agreement. Since 1998, the city's affordable housing program functions, which include monitoring unilateral agreement requirements, have been performed by the Department of Planning and Permitting. Prior to 1998, the former Department of Land Utilization and Department of Housing and Community Development administered the affordable housing program.

Under current departmental rules, developers have options in meeting affordable housing requirements imposed by unilateral agreements:

- Construct affordable housing units for sale or rent on the re-zoned project site.
- Construct affordable housing units for sale on property other than the re-zoned project site.
- Provide finished house lots for owner-builder efforts.
- Convey improved or unimproved land, on- or off-site, suitable for affordable housing construction.
- Contribute a cash or “in-lieu” fee based on a set formula.

In addition to the affordable housing options established by rule, the city may allow developers to utilize excess affordable housing credits earned under a unilateral agreement to meet affordable housing requirements imposed by another unilateral agreement.

Planning guidelines for O‘ahu’s future development and residential growth are established in the city’s General Plan, Sustainable Communities Plans, and Development Plans. For example, the general plan’s housing policies support financial and other incentives to encourage the private sector to build homes for low- and moderate-income residents, and to distribute low- and moderate-income housing fairly throughout the island. The development and sustainable communities plans cover eight areas on O‘ahu: Central O‘ahu, Ewa, Primary Urban Center, East Honolulu, Ko‘olaupoko, Ko‘olauloa, North Shore, and Wai‘anae. Plans representing these eight areas also establish affordable housing goals and objectives.

Summary of Findings

1. The department of planning and permitting’s administration of unilateral agreements for affordable housing is inadequate. The department lacks a formal unilateral agreement monitoring program for affordable housing, does not maintain an accurate, verified inventory of affordable housing units built under unilateral agreements, and has not maintained historical data on unilateral agreements and its requirements.

2. In-lieu fee collections have not resulted in affordable housing benefits for the 80-120 percent of median income group. Since 1998, in-lieu fees have not been expended for affordable housing-related purposes. The Housing Development Special Fund, which holds in-lieu fees, is not specifically intended for the development of affordable housing and limits the city's ability to expend in-lieu fees. Acceptance of in-lieu fees may be inconsistent with current general, development, and sustainable community plans related to affordable housing.
3. Accumulating and redeeming affordable housing credits are not formalized in ordinance or rule. The department of planning and permitting authorized developers to accumulate affordable housing credits contrary to city ordinance under a moratorium on affordable housing conditions. The department's excess affordable housing credit application practices are generally consistent with general, development, and sustainable community plans related to affordable housing, but may conflict with the general plan's housing objective advocating diverse communities.

Finding 1: The Department of Planning and Permitting's Administration of Unilateral Agreements in Affordable Housing is Inadequate

- We found that the department has not established an effective affordable housing unilateral agreement monitoring program. Because the department's unilateral agreement administration is inconsistent and reactionary in nature, the department has not proactively verified developer compliance with unilateral agreement requirements.
- The department does not maintain an accurate, verified inventory of affordable housing. We found that planning and permitting staff rely on an affordable housing database that was last updated in 2000 and that poor record-keeping practices hamper the department's ability to assess developer compliance. The department also reports unverified and flawed affordable housing data to the council and public.
- The department does not maintain historical affordable housing data. The department claims that since unilateral agreement conditions in affordable housing began in the 1970s, the city has constructed

nearly 13,000 affordable housing units for sale or rent. However, the city is unable to provide data to verify this claim.

- Inadequate staffing is blamed for poor monitoring. The department notes that it assumed unilateral agreement monitoring responsibilities in 1998 as the result of a reorganization of city government. The department did not receive any additional staff or resources to take on this responsibility. Between 1999 and 2002, five staff persons were assigned to unilateral agreement monitoring. Currently, the department has one full-time staff person assigned to monitor unilateral agreements in affordable housing.

Finding 2: In-lieu Fee Collections Have Not Resulted in Affordable Housing Benefits as Intended

- Since 1998, no in-lieu fees were expended for affordable housing related purposes. Between FY1992-93 to FY2005-06, the city collected nearly \$4.5 million in in-lieu fees. We found that at least \$3.2 million in in-lieu fees from the former Housing Assistance Fund were directed into the city's general fund instead of being spent on affordable housing initiatives. In 2004, the former budget and fiscal services director reported that the in-lieu fee balance was \$391,371. By lapsing in-lieu fees from the Housing Assistance Fund and the Housing Development Special Fund into the general fund, the city adversely impacted the housing development special fund's future effectiveness. We also found that there are no plans, goals, or objectives for spending in-lieu fees.
- The housing development special fund is not specifically intended for the development of affordable housing. The purpose of the fund is the development of housing for sale or rent, with no specific reference to *affordable* housing. Thus, the city cannot be assured that in-lieu fees will be used for affordable housing purposes. We also found that no specific agency is tasked to monitor, plan, or expend in-lieu fees collected from developers. As a result, in-lieu fees may have been expended for purposes other than housing.
- The current framework for the collection of in-lieu fees is inadequate for significant development of affordable housing for sale or rent. With a current balance of \$820,000, the housing development special fund cannot develop a significant amount of affordable housing for sale or rent. We also found that communities affected by

zoning changes do not directly benefit from in-lieu fee collections. Hawai'i county amended its in-lieu fee program due to the lack of affordable housing units built.

- The acceptance of in-lieu fees may be inconsistent with current general, development, and sustainable community plans related to the construction of affordable housing units. We found that compliance with general, development, and sustainable communities plans related to affordable housing is not documented. Limitations on the use of in-lieu fees do not support the plans' affordable housing objectives.

Finding 3: The Department of Planning and Permitting's Authorization and Application of Excess Affordable Housing Credits Lack Accountability

- Accumulating and redeeming excess affordable housing credits are not formalized in ordinance or rule. In practice, the planning and permitting department credits developers for affordable housing construction that exceeds the minimum required under unilateral agreements. These *excess* credits may be used to satisfy future affordable housing requirements. We found, however, that affordable housing credits are not tracked to determine a developer's balance, sale, or redemption of excess affordable housing credits. Unlike the City and County of Honolulu, Hawai'i and Maui counties codify the use of affordable housing credits.
- The department authorized developers to accumulate excess affordable housing credits contrary to city ordinance under a moratorium on affordable housing conditions. We found that Ordinance 99-51 provided relief to developers during a market downturn. The ordinance placed a moratorium on affordable housing conditions imposed by the city so that developers could sell their affordable housing inventory and meet unilateral agreement requirements. However, the planning and permitting department allowed developers to bank affordable housing credits in excess of the minimum requirements imposed by unilateral agreement. Redemption of excess credits earned during the moratorium may conflict with the intent of the city's affordable housing program.
- The department's excess affordable housing credit practices may conflict with the general plan's housing objective advocating diverse communities. Incentives to construct more affordable housing units are consistent with general, development, and sustainable

communities plans provisions in affordable housing. However, application of excess credits may conflict with the general plan's housing objective that encourages the fair distribution of low- and moderate-income housing throughout the island.

Recommendations and Response

We made several recommendations to the Department of Planning and Permitting to improve its effectiveness and efficiency in administering unilateral agreements for affordable housing. We recommended that the department establish formal policies and procedures for administering unilateral agreements, including monitoring requirements. We also suggested that the department maintain a matrix or database with accurate, verifiable data, including historical data of all affordable housing units built under unilateral agreements. In addition, we recommended that the department amend its rules by establishing an in-lieu fee formula that is consistent with established goals and objectives, and by proposing a framework for the accrual and application of excess affordable housing credits. We also suggested that the department establish procedures to document how the delivery options exercised by developers conform to general, development, or sustainable community plan provisions related to affordable housing. Additionally, we urged the department to report verified affordable housing data in its annual report to the council as required by city ordinance. Finally, we recommended that the department evaluate its staffing allocation for unilateral agreement monitoring and to ensure compliance with future unilateral agreement provisions.

We also recommended that the Honolulu City Council consider amending Section 6-46.2, Revised Ordinances of Honolulu, to specify that in-lieu fees deposited into the Housing Development Special Fund shall be used for affordable housing-related purposes, to clarify and expand the use of in-lieu fees, and to designate a city agency to monitor, plan, and expend in-lieu fees. We also recommended that the council consider further review of the housing development special fund's expenditures.

In its response to our draft report, the Department of Planning and Permitting expressed concerns that confidential copies of the draft report were provided to others outside of the department and mayor's office, that the audit was inconsistent with the original intent of Resolution 05-285, CD1, and that the draft report contained errors and inaccuracies. We note that some of the department's comments,

presented as errors or inaccuracies, were clarifying information that enhanced the report, but did not have a substantive effect on the audit findings and recommendations. In other instances, the department commented on issues outside the scope of this audit. We also noted that some of the purported errors and inaccuracies were based on information provided to us by department staff or the result of information that the department failed to disclose to us during fieldwork. In those instances, the additional information did not have a material effect on our audit findings. However, we acknowledge the validity of some of the department's comments and have amended the final report to ensure accuracy and clarity. Finally, the department concurred with the following problems revealed in our audit report: that staffing shortages and competing priorities have resulted in the department using subdivision application or building permit review for unilateral agreement compliance instead of monitoring annual reports; that the state of documentation, archiving, and retrieval of documentation is a challenge; that the backlog in reviews and certifications of developer's submittals for affordable housing credits have been reduced; and that the departmental rules used for administering the affordable housing agreements need to be updated.

The department also provided several comments on substantive issues that merited a response. For these issues, we explained that information we reviewed supported a contrary view or that data was not provided to us during fieldwork. We also note that the Department of Budget and Fiscal Services declined to submit a separate response to our draft audit report and instead relied on the planning and permitting department to respond on its behalf.

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Chapter 1

Introduction

This audit was conducted pursuant to Resolution 05-285, CD1, *Requesting the City Auditor to Audit the City's Affordable Housing Program*, which was adopted by the Honolulu City Council on October 19, 2005. The audit is included in the Office of the City Auditor's Annual Work Plan for FY2006-07 as communicated to the council and mayor in June 2006. While the resolution's title implies an audit of the city's broader affordable housing program, we focused our review on issues raised in the resolution pertaining to affordable housing conditions in unilateral agreements.

The purpose of the resolution is to have the city auditor objectively review, evaluate, and improve the city's affordable housing program. Through Resolution 05-285, CD1, the council requested that the city auditor address issues including, but not limited to:

1. The effectiveness and efficiency of the city's use of affordable housing conditions in unilateral agreements, such as buyback and shared appreciation conditions, in achieving the stated goals and objectives of the city's General Plan and Development Plans relating to affordable housing programs;
2. The adequacy of current staffing to monitor, administer, and enforce the affordable housing conditions of unilateral agreements; and
3. The appropriateness of the selling prices of affordable housing units developed pursuant to the affordable housing provisions of unilateral agreements.

During our preliminary review, we found that since 2005, many government and housing industry groups have provided substantial information regarding buyback and shared appreciation conditions. Furthermore, we identified developers' payment of in-lieu fees and application of excess affordable housing credits as having potentially more significant impact on the city's affordable housing program, and the least amount of information provided publicly. In-lieu fees are cash payments made by developers instead of constructing affordable housing units. Excess affordable housing credits are credits earned beyond the minimum required by unilateral agreement, which can be applied to meet future affordable housing requirements.

Rather than reexamine issues that have already been reported, we departed from the resolution’s focus on shared appreciation and buyback restrictions and instead assessed the effectiveness of in-lieu fees and excess affordable housing credits granted by the Department of Planning and Permitting as they relate to the city’s affordable housing program. Additionally, we note that shared appreciation and buyback restrictions may not directly affect the number of affordable housing units built because they are imposed after-the-fact on affordable housing units already constructed, whereas in-lieu fees and excess affordable housing credits directly affect the number of affordable housing units *actually* built. Not only does this amended focus retain the resolution’s intent to examine the city’s efforts to increase the supply of affordable housing through unilateral agreements attached to zone change ordinances, but also provides the council and public with new information on unilateral agreements requiring affordable housing.

Background

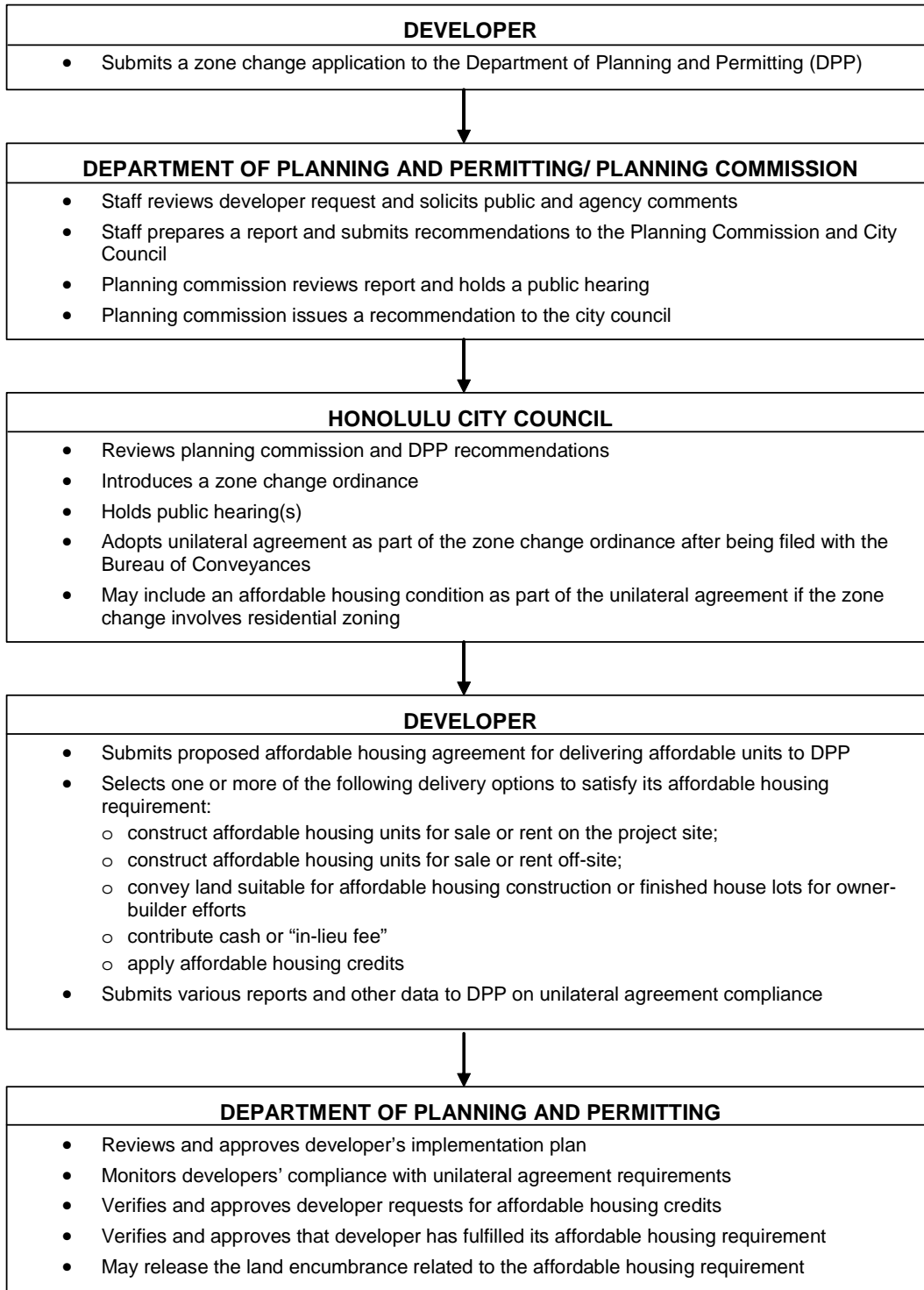
During the 1970s local governments across the country began implementing “inclusionary zoning” or “inclusionary housing,” which required developers to set aside a certain percentage of housing units for low- and moderate-income households within otherwise market-rate developments. At the same time, the City and County of Honolulu began imposing various requirements on developers who requested land use rezoning to ensure the production of affordable housing through “unilateral agreements” by ordinance. In 1994, the former Department of Housing and Community Development adopted rules for unilateral agreements requiring affordable housing. The city’s initiatives in affordable housing are also guided by general, development, and sustainable communities plans, which establish a policy context for the city’s land use and budgetary actions.

City ordinance establishes conditional zoning or “unilateral agreements”

Section 21-2.80, Revised Ordinances of Honolulu, *Conditional Zoning—Agreements*, provides that before the enactment of an ordinance for a zone change, the city council may impose conditions on the applicant’s use of the property. The fulfillment of these conditions shall be a prerequisite to the adoption of the ordinance or any applicable part. This section further provides that the conditions shall be set forth in a unilateral agreement running in favor of the council, acting by and through its chair. The agreement shall be enforceable by the city.

Affordable housing requirements are established in unilateral agreements. A unilateral agreement is defined as *a covenant running with the land prepared, executed, and recorded in the Bureau of Conveyances, State of Hawai‘i, by the owner of the real property for which a zone change is requested and incorporated into, and made a part of, the ordinance effecting the zone change which states the condition under which a developer has agreed to use that real property.* Exhibit 1.1 depicts the process of incorporating affordable housing conditions by the zone change process through unilateral agreements.

**Exhibit 1.1
Flowchart of Unilateral Agreement For Affordable Housing**



Source: Office of the City Auditor and the Department of Planning and Permitting

Affordable housing requirements are imposed by unilateral agreements and rules

In 1994, the former housing and community development department adopted *Rules for the Terms of Unilateral Agreements Requiring Affordable Housing*. The rules establish general application, terms and conditions, applicant qualifications, selection criteria, restrictions on the transfer, sale, buyback, use of affordable properties, and reporting requirements. In addition to the requirements established by rule, the council may impose its own requirements through a zone change ordinance. Council-imposed requirements may be in addition to, or supersede, requirements established by rule. Prior to 1994, unilateral agreements were more descriptive and affordable housing requirements varied because they were imposed on a project-by-project basis. With the establishment of rules, developers could anticipate some of the expectations in unilateral agreements.

The city's affordable housing initiatives are primarily targeted at two income groups. The low-income household group is defined as a household whose income does not exceed 80 percent of the median income for the Honolulu Metropolitan Statistical Area as determined by the U.S. Department of Housing and Urban Development (HUD), adjusted for household size. The moderate-income household category is defined as a household whose income is greater than 80 percent, but does not exceed 120 percent of the median income within the same criteria.

The current rules typically require that the number of affordable housing units sold or rented to low- and moderate-income households comprise a minimum of 30 percent of the total number of residential units planned for construction in a project area. The rules further provide that at least 10 percent of the residential units planned for construction in the project area shall be sold or rented to households earning 80 percent or less of the median income for the Honolulu Metropolitan Statistical Area.

Developers have options in fulfilling affordable housing requirements

Under current rules, a developer may satisfy an affordable housing requirement by providing one or more of the following options that the planning and permitting department deems acceptable:

- Construct affordable housing units for sale. Housing units are constructed on the rezoned project site for sale at prices determined by a preset formula. Owners must reside in the unit for a minimum of one year in order for the developer to receive a credit for the affordable unit.

- Construct affordable housing units for rent. Rental units are constructed on the rezoned project site at established rental rates. The rental units must be rented for a minimum of 10 years in order for the developer to receive a housing credit. After 10 years, the city has the right-of-first-refusal to purchase the project. Affordable units rented to low-income households for more than 20 years may be eligible for enhancement credits as determined by the department.
- Provide finished house lots. Developer may provide finished house lots for affordable housing owner-builder efforts under guidelines established by the department.
- Convey land. The developer may convey improved or unimproved fee simple or leasehold real property on or off the project site, zoned and suitable for the construction of affordable housing units. The land's appraised value must be equal to the in-lieu cash payment provided for by rule.
- Construct for-sale or rental units off-site. Developers may construct affordable housing units on a site other than the real property described in the rezoning ordinance. Rental units must be rented for a minimum period of 10 years and the city has the right-of-first-refusal to purchase the project after the ten-year period and the developer opts to sell.
- Contribute cash or "in-lieu" fee. The developer may provide an in-lieu fee equal to the difference between the estimated cost of building the affordable housing unit, less the unit's estimated sales price at the time the in-lieu payment is due.

In addition to the six delivery options provided by rule, the Department of Planning and Permitting may allow developers to satisfy affordable housing requirements by applying excess affordable housing credits earned at a different development project. The department's policy allows developers the option to utilize credits if: 1) the project site is within the same development plan district as the project site where the credit will be applied; and 2) the project site is within a 7.5 mile radius of the project site.

Affordable housing credits are based on a sliding scale

Under the current rules, developers earn affordable housing credits based on the type of affordable housing unit built. For example, a developer would receive 1.00 credit for constructing a two-bedroom/one-and-a-half bath unit; a one-bedroom/one-bath unit would earn 0.81 credits; and a three-bedroom/two-bath unit would earn 1.44 credits. A developer may satisfy the total affordable housing requirement by producing any acceptable combination of affordable housing units which will equal or exceed its minimum requirement. Prior to the adoption of the rules in 1994, unless a unilateral agreement specified otherwise, developers earned one affordable housing credit for each affordable housing unit constructed (one-for-one), regardless of size, type, or configuration. Exhibit 1.2 provides the factor table used to calculate affordable housing credits under departmental rules.

Exhibit 1.2
Affordable Housing Credit Factor Table

	<i>Type of Unit Built</i>							
	0 Bedroom 1 Bath	1 Bedroom 1 Bath	2 Bedroom 1 Bath	2 Bedroom 1.5 Bath	2 Bedroom 2 Bath	3 Bedroom 1.5 Bath	3 Bedroom 2 Bath	3+ Bedroom 2+ Bath
Affordable Housing Credit Earned	0.68	0.81	0.92	1.00	1.08	1.16	1.28	1.44

Source: Rules for the Terms of Unilateral Agreements Requiring Affordable Housing, 1994

Developer's implementation plan requires approval

Current rules also require developers to prepare an implementation plan acceptable to the planning and permitting department for the delivery of affordable housing units. The department must approve the plan prior to construction. The implementation plan must contain the following information:

- location of the affordable housing units;
- types of affordable housing units to be constructed (e.g. three-bedroom, two-bath unit) and supporting information which justifies the types of bedroom mix;

- price of affordable housing units; and
- delivery schedule of all market and affordable housing units for each phase of the project under the unilateral agreement.

General plan establishes long-range growth for O‘ahu

The General Plan for the City and County of Honolulu, a requirement under the city charter, is a comprehensive statement of objectives and policies which establishes the long-range aspirations of O‘ahu’s residents and the strategies to achieve them. The plan is the focal point of a comprehensive planning process that addresses physical, social, economic, and environmental concerns affecting the city, and guides future growth for metropolitan Honolulu.

The General Plan guides all levels of government, private enterprise, neighborhood and citizen groups, organizations, and individual citizens in eleven areas:

1. Population
2. Economic activity
3. Natural environment
4. Housing
5. Transportation and utilities
6. Energy
7. Physical development and urban design
8. Public safety
9. Health and education
10. Culture and recreation
11. Government operations and fiscal management

The general plan’s housing policy acknowledges that obtaining decent, reasonably priced homes in safe and attractive neighborhoods has been a perennial problem for the residents of O‘ahu. The plan’s objectives and

policies for housing seek to provide a choice of living environments, affordable housing, and a reduction of inflationary speculation. The general plan's first housing policy objective is to provide decent housing for all the people of O'ahu at prices they can afford. The plan's housing policies seek to:

- develop programs and controls which will provide decent homes at the least possible cost;
- provide financial and other incentives to encourage the private sector to build homes for low- and moderate-income residents;
- encourage the preservation of existing housing which is affordable to low- and moderate-income persons;
- encourage the production and maintenance of affordable rental housing;
- encourage residential developments that offer a variety of homes to people of different income levels and to families of various sizes;
- encourage the fair distribution of low- and moderate-income housing throughout the island; and
- preserve older communities through self-help, housing-rehabilitation, improvement districts, and other governmental programs.

Development and sustainable communities plans guide land-use policies for growing and established communities

In addition to the general plan, development and sustainable communities plans also guide public policy, investment, and decision-making, specifically over a 25-year period. Developed with community participation, each plan addresses one of the eight planning regions of O'ahu and responds to the specific conditions and community values of each region. The eight plan areas include Central O'ahu, Ewa, Primary Urban Center, East Honolulu, Ko'olaupoko, Ko'olauloa, North Shore and Wai'anae, and are depicted in Exhibit 1.3.

Exhibit 1.3
Development Plan and Sustainable Communities Plan Areas on O‘ahu



Source: Department of Planning and Permitting

Plans for Ewa and the Primary Urban Center, to which growth and supporting facilities will be directed over the next two decades, are titled, “Development Plans.” They serve as the policy guide for development decisions and actions needed to support that growth. Plans for the remaining six areas, which are envisioned as having relatively stable growth regions and focus on supporting existing populations, are titled “Sustainable Communities Plans” in order to appropriately indicate their intent. Although each of the eight plans addresses the distinct needs of the communities they represent, all plans express a desire for some form of affordable housing, including low- and moderate-income sectors.

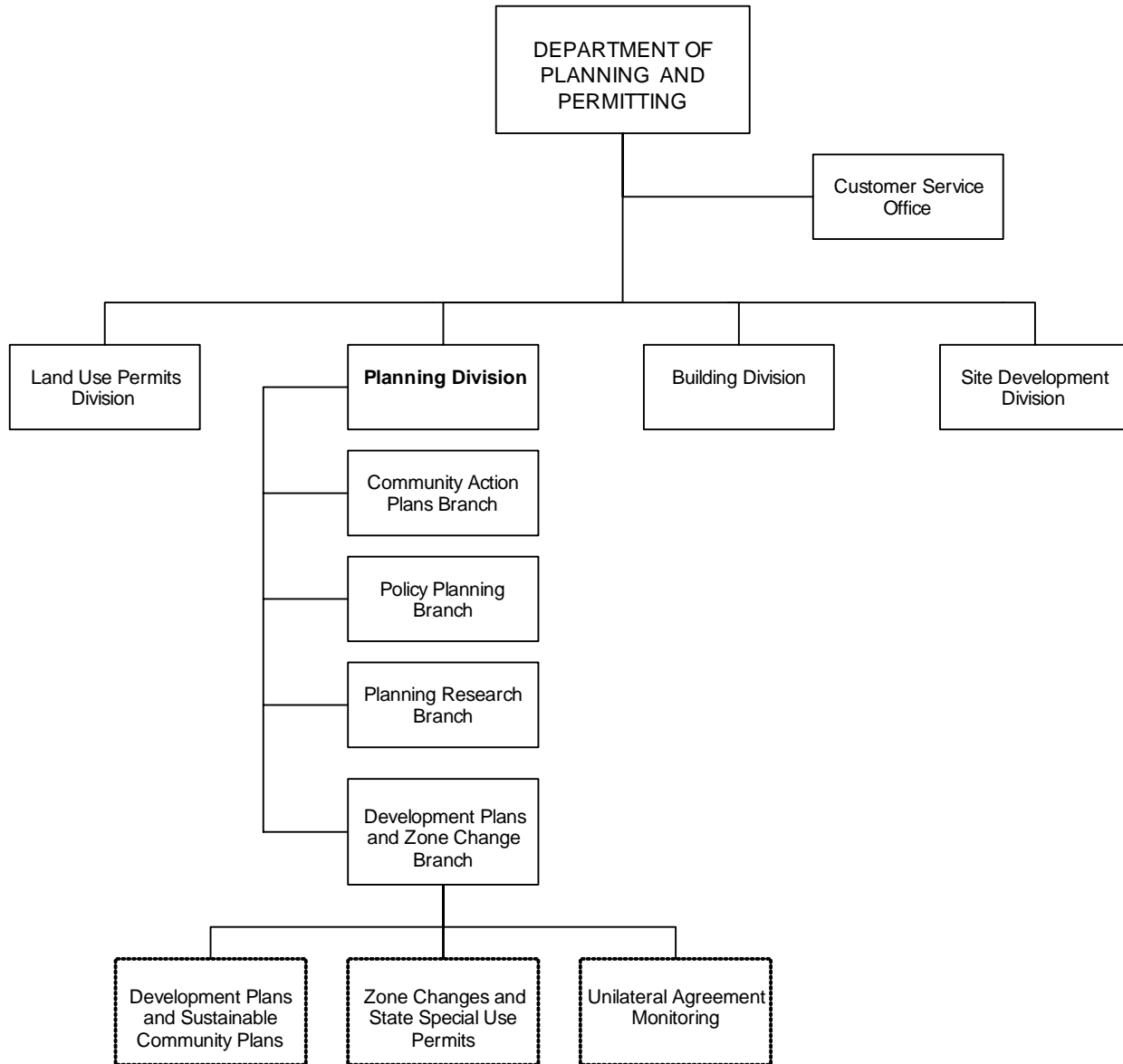
The City's Unilateral Agreements for Affordable Housing are Managed by the Departments of Planning and Permitting and Budget and Fiscal Services

The Department of Planning and Permitting administers unilateral agreements in affordable housing by monitoring developer compliance with agreement requirements. The department inherited this responsibility from the former Department of Housing and Community Development, which was dissolved during the city-wide reorganization in 1998. In addition, the Department of Budget and Fiscal Services collects fees associated with the affordable housing program and administers the Housing Development Special Fund.

Department of Planning and Permitting administers unilateral agreements in affordable housing

The Department of Planning and Permitting is responsible for the city's long-range and community planning efforts, and for the administration and enforcement of various permits required for development and land use, codes pertaining to the construction of buildings, and various city standards and regulations pertaining to infrastructure requirements. The department consists of four functional divisions: planning, land use permits, site development, and building. Exhibit 1.4 presents the department's organizational structure.

Exhibit 1.4
Department of Planning and Permitting Organizational Chart as of December 2006



Source: Department of Planning and Permitting

The department's Planning Division is responsible for the preparation, evaluation, and revision of the O'ahu General Plan and the eight long-range regional development and sustainable communities plans. It also monitors the status of unilateral agreement conditions, including affordable housing program requirements. In addition, it develops community-based special area plans, prepares an annual report on

current status of land use, and assists infrastructure agencies in preparing functional plans to assure consistency with land use plans. Prior to FY2004-05, these functions were performed by the Planning and Zoning Program. Exhibit 1.5 provides the planning division's staffing, expenditure, and funding data for FY2003-04 to FY2005-06.

Exhibit 1.5
Planning Division Budgeted Positions, Expenditures, and Funding Sources,
FY2003-04 to FY2005-06

	<i>FY2003-04*</i>	<i>FY2004-05</i>	<i>FY2005-06</i>
Program Positions (FTE)			
Permanent Positions	N/A	27.00	27.00
Temporary Positions	N/A	0.00	0.00
Contract Positions	N/A	0.00	0.00
TOTAL	N/A	27.00	27.00
Expenditures			
Salaries and Wages	N/A	\$1,167,246	\$1,292,672
Current Expenses	N/A	\$163,635	\$528,635
Equipment	N/A	\$0	\$0
TOTAL	N/A	\$1,330,881	\$1,821,307
Funding Source			
General Fund	N/A	\$1,280,881	\$1,821,307
Community Development Fund	N/A	\$50,000	\$0
TOTAL	N/A	\$1,330,881	\$1,821,307

* In FY2003-04, the Planning Division was called the Planning and Zoning Program

Source: City and County of Honolulu Operating Budget

The department's Development Plans and Zone Change Branch monitors and enforces unilateral agreements

The planning division's Development Plans and Zone Change Branch is tasked with administering development and sustainable communities plans, zone changes and state special use permits, and unilateral

agreement monitoring. As of March 2007, the department of planning and permitting's records indicate that it, and its predecessor agency, the department of housing and community development, have monitored 185 unilateral agreements going as far back as 1973. These agreements include conditional requirements for both commercial and residential zone changes under unilateral agreements. As of June 30, 2006, the department reported that it is tracking 47 unilateral agreements with affordable housing requirements.

The branch ensures developer compliance with unilateral agreement requirements. In addition to reviewing annual reports submitted by developers, branch staff are responsible for conducting annual reviews of housing projects with affordable housing requirements to assess developers' compliance status. If a developer is not in compliance, staff will communicate with the developer and request compliance; otherwise, the planning and permitting department may withhold building permit approvals until compliance is met.

City-wide reorganization in 1998 assigned monitoring duties to the planning and permitting department

Prior to 1998, the Department of Land Utilization and Department of Housing and Community Development administered unilateral agreements. As a result of a city-wide reorganization of executive branch agencies, the agencies were dissolved and their responsibilities dispersed among the current planning and permitting, budget and fiscal services, and community services departments. Since 1999, the department of planning and permitting has actively managed unilateral agreements.

Budget and fiscal services manages in-lieu fees collected under unilateral agreements

As the city's central financial agency, the budget and fiscal services department is responsible for all aspects of the city's finances, including billing, collection, keeping accurate and complete account of receipts and disbursements, and management of the city's treasury and funds. The department also reviews the manner in which public funds are received and expended, and reports on the integrity with which public funds are accounted for. Thus, the department's responsibilities also include depositing, managing, and accounting for in-lieu fees collected from developers, which are placed in the housing development special fund.

In-lieu fees are deposited into the Housing Development Special Fund

Section 6-46.1, ROH, establishes the Housing Development Special Fund. The fund's purpose is to develop housing for sale or for rent in the City and County of Honolulu. Generally, this fund accounts for general obligation bond proceeds and bond anticipation notes authorized and issued for the purpose of developing housing. The fund also accounts for the proceeds from the sale or rental of housing. Although in-lieu fees are deposited into the housing development special fund, Section 6-46.3, ROH, does not specifically identify in-lieu fees as a fund source. From FY 1992-93 to FY 2005-06, budget and fiscal services reports that it collected \$4,461,440 in in-lieu fees. At the end of FY 2005-06, the housing development special fund balance was \$13,673,312.

Audit Objectives

1. Assess the effectiveness and efficiency of the Department of Planning and Permitting's management of developer credits and in-lieu fees under unilateral agreements in achieving the goals and objectives of the city's general plan, development plans, and sustainable communities plans related to affordable housing.
2. Make recommendations as appropriate.

Scope and Methodology

We focused our review on the Department of Planning and Permitting's authorization and management of affordable housing credits and in-lieu fees under unilateral agreements from FY 1998-99 through May 2007. When deemed appropriate, we also reviewed data prior to FY 1998-99. We assessed the planning and permitting department's compliance with applicable laws, ordinances, rules, policies, and procedures relating to unilateral agreements. We examined the department of planning and permitting's unilateral agreement monitoring activities, internal controls, data management, and adequacy of staffing. We also assessed whether in-lieu fees and excess affordable housing credits have produced results consistent with the goals and objectives of the general, development, and sustainable community plans. Additionally, we compared the department's policies, procedures, and administration of unilateral agreements in affordable housing with similar programs administered by Hawai'i, Kaua'i, and Maui counties.

We also assessed the Department of Budget and Fiscal Services' administration of the former Housing Assistance and current Housing

Development Special Funds, which were the repositories for in-lieu fees paid by developers. We analyzed fund collections and disbursements, identified the amount of in-lieu fees collected by the city from FY1992-93 to FY2005-06, how the fees were spent, and determined if the fees were spent in accordance with city ordinance, policies, or procedures.

In addition, we interviewed applicable administrators and staff of the departments of planning and permitting, and budget and fiscal services. We also interviewed representatives from development companies that have constructed affordable housing units under a unilateral agreement requirement. Finally, we interviewed housing department administrators from Hawai‘i and Kaua‘i counties.

This audit was conducted in accordance with generally accepted government auditing standards.

Chapter 2

The Department of Planning and Permitting's Administration of Affordable Housing Conditions is Inadequate and Better Scrutiny of In-lieu Fees and Affordable Housing Credits is Needed to Increase the Number of Affordable Housing Units Actually Built

In June 2007, the median price of a single family home on O‘ahu was \$685,000, up 7.2 percent from \$639,000 in June 2006. The median price for a condominium during the same time period was \$334,000, up 7.7 percent from \$310,000 from the same month in the previous year. Oftentimes, these market-priced homes are out of reach for many families and individuals. As a result of the high cost of homeownership, elected officials and agencies from all branches of government operate programs designed to meet the increasing need for affordable housing on O‘ahu. Despite the public’s outcry to solve affordable housing issues, and the high priority placed on this dilemma, we found that the city’s efforts have fallen short. While the city is currently performing affordable housing *functions*, it lacks any formal program with measurable goals or objectives. We found that the city’s current administration of unilateral agreements in affordable housing lacks a formal structure, an accurate inventory, or other important data needed to fully assess the city’s effectiveness in meeting affordable housing goals. Also, the city’s current practices of collecting in-lieu fees and application of housing credits have impacted the number of affordable housing units actually constructed. Finally, the city has failed to effectively administer the Housing Development Special Fund and the resources earmarked for affordable housing needs.

Summary of Findings

1. The department of planning and permitting’s administration of unilateral agreements for affordable housing is inadequate. The department lacks a formal unilateral agreement monitoring program, does not maintain an accurate, verified inventory of affordable housing units built under unilateral agreements, and has not

maintained historical data on unilateral agreements and its requirements.

2. In-lieu fee collections have not resulted in affordable housing benefits for the 80-120 percent of median income group. Since 1998, in-lieu fees have not been expended for affordable housing-related purposes. The Housing Development Special Fund, which holds in-lieu fees, is not specifically intended for the development of affordable housing and limits the city's ability to expend in-lieu fees. Acceptance of in-lieu fees may be inconsistent with current general, development, and sustainable community plans related to affordable housing.
3. Accumulating and redeeming affordable housing credits are not formalized in ordinance or rule. The department of planning and permitting authorized developers to accumulate affordable housing credits contrary to city ordinance under a moratorium on affordable housing conditions. The department's excess affordable housing credit application practices are generally consistent with general, development, and sustainable community plans related to affordable housing, but may conflict with the general plan's housing objective advocating diverse communities.

The Department of Planning and Permitting's Administration of Unilateral Agreements in Affordable Housing is Inadequate

The department has not established an effective affordable housing unilateral agreement monitoring program

The department of planning and permitting's administration of unilateral agreements for affordable housing is inadequate. The department lacks a formal unilateral agreement monitoring program for affordable housing conditions, does not maintain a current, accurate, verified inventory of affordable housing units built under unilateral agreements, and has not maintained historical data on unilateral agreements and its requirements related to affordable housing. As a result, the city cannot be assured that unilateral agreement requirements for affordable housing are being met nor does it maintain necessary information to assess the effectiveness of those agreements.

Unilateral agreements and applicable departmental rules establish a variety of requirements that developers must meet to maintain compliance and proceed with project construction. Thus, a unilateral agreement functions much like a contract in that parties enter into an agreement for specific deliverables at designated intervals. Contracting best practices require government agencies to actively monitor and

evaluate contractors to ensure that such requirements are met. We found, however, that the planning and permitting department's monitoring activities are inconsistent and ineffective in ensuring that unilateral agreement and applicable rule requirements are being met.

Unilateral agreement administration is inconsistent and reactionary in nature

The department of planning and permitting does not have formal, written policies and procedures for monitoring unilateral agreements. We found a reference to 1983 Department of Housing and Community Development guidelines in a unilateral agreement file, but a current planning division administrator was unfamiliar with these guidelines and did not have a copy. In practice, the department monitors unilateral agreements in two primary ways. First, department staff complete a monitoring report, which identifies unilateral agreement requirements and the developer's status in complying with those requirements. According to the division, this monitoring report should be completed annually. However, due to staff constraints, since 2000, monitoring reports are generally completed only when a developer is seeking approval for a building permit. A planning division administrator acknowledged that the department's monitoring practices can best be described as "reactionary." The division administrator reported that every permit application is an opportunity to assess a developer's compliance with unilateral agreement requirements and, if compliance is not met, the department can withhold permit approval until the developer complies. In our view this practice is problematic because significant periods of time may elapse between permit approval requests. Developer non-compliance with unilateral agreement requirements may be on-going and the department may not be aware of it until the next permit application review. This may adversely impact the project and compromise the department's ability to ensure that requirements are met in a timely manner. Rather than react to a permit approval request, the department should be monitoring developer compliance with unilateral agreement requirements and taking appropriate action at regular intervals.

Second, Section 21-2.80, Revised Ordinances of Honolulu, requires developers to submit annual reports detailing the status of its compliance with unilateral agreement conditions. Planning Division staff are supposed to review these reports and evaluate developer compliance. If a developer fails to submit an annual report, the department may withhold a building permit and other approvals until the report is submitted. We found, however, that developers do not routinely submit annual reports. We reviewed zone change files for 18 development

projects with affordable housing conditions and found that none of the files contained annual reports for each year a report should have been filed. We also spoke to representatives from three development companies that were required to submit annual reports under unilateral agreements and they, too, acknowledged that annual reports were not consistently filed. Although the department had the authority to withhold a permit approval, we found that division staff did not always withhold permits from developers for failure to submit an annual report.

Because the department did not conduct its own unilateral agreement monitoring at consistent intervals, the annual reports submitted by developers would have provided the department an indication of developers' compliance. However, since annual reports were not always submitted, we find it difficult to determine how the planning and permitting department could make accurate assessments about developers' compliance with unilateral agreement requirements. In one instance, we found an annual report in the unilateral agreement files that was photocopied in a "mirror" image, which rendered the report unreadable. We question whether the department actually reads the developer reports or merely place them in the files.

The department has not proactively verified developer compliance with unilateral agreement requirements

Division administrators acknowledge that one of the monitoring activities that the department used to do, but no longer does consistently, are field investigations to verify developer submissions. While the department of planning and permitting diligently verifies income and occupancy requirements for buyers of affordable homes constructed under unilateral agreements, other requirements are not always verified. For example, a common affordable housing unilateral agreement requirement is that affordable units should look similar to market units, and not stand out. A simple drive by the community could determine compliance with this provision. However, the department claims that it does not have the time or resources to verify that such requirements are met.

Prior to the planning division's administration of unilateral agreements, the former land utilization department's Monitoring and Compliance Branch monitored zone change conditions, including unilateral agreements. According to a former branch administrator, the branch put forth a great deal of effort to monitor unilateral agreements, especially affordable housing conditions because it was such an important issue to the council and administration. The branch verified all unilateral agreements annually and provided annual reports to the council on the

status of all zone change conditions. The branch's five staff members would also conduct site visits to verify claims made by developers in their annual or other reports.

The department does not maintain an accurate, verified inventory of affordable housing

Accurate records enable and support an agency's work to fulfill its mission. Since affordable housing records comprise various information, it is essential to take a systematic approach to managing such records. Adequate recordkeeping contributes to the smooth operation of the agency's programs by making the information needed for decision making and operations readily available. It also helps deliver services in a consistent and equitable manner, and ensures compliance with statutory and regulatory requirements including archival, audit, and oversight activities. We found, however, that the department of planning and permitting has not adequately managed affordable housing unilateral agreement records, which adversely impacts its ability to administer those agreements.

Staff rely on a database that was last updated in 2000

The department of planning and permitting does not maintain an updated database of unilateral agreements with affordable housing requirements or the status of developers' compliance. According to planning division staff, the department used to maintain a running spreadsheet identifying unilateral agreements in affordable housing and compliance status since it assumed the responsibility for monitoring unilateral agreements in 1998. However, this practice stopped in 2000 due to lack of staff, time constraints, and other department priorities. The planning division staff responsible for monitoring unilateral agreements estimates that it would take two staff persons 400 work hours to research and update the 2000 list. Because the department no longer keeps a running database of unilateral agreement requirements, it cannot effectively monitor nor readily provide pertinent information to developers, the council, or the public.

We posed the following question to a division administrator and staff assigned to monitor unilateral agreements:

At any given time, can you identify 1) a developer's affordable housing requirement, 2) how many affordable housing units the developer has constructed, and 3) the outstanding number of housing units/credits?

The key staff person in charge of monitoring unilateral agreements in affordable housing responded that it could not be done immediately and would require staff to dig into hard copy files or POSSE (Public One Stop Service), which is used by the department as its permit management and tracking system. Also, there are no standard procedures for information intake. The division administrator commented that it would take two to three months, referring to the amount of time it would take to identify and verify the number of units already constructed and the number of outstanding units to be built. The administrator further explained that the current data system is not set up to maintain historical data and that staff from the former housing and community development department maintained personal databases that may have contained important information. However, much of that information was lost due to retirement or separation from the city.

In one instance, we found that on October 6, 2003, a developer submitted in-lieu fees totaling \$118,552 and requested a release from its affordable housing requirements. However, the planning and permitting department did not respond to the developer's request until eight months later, on June 22, 2004. In its response, the department determined that the developer had already met its affordable housing requirements under its unilateral agreement and returned the fee payment to the developer. If the department had been proactive and maintained accurate, verified records of affordable housing requirements, it could have addressed this issue sooner. Without accurate records, the department's credibility in ensuring that requirements are, in fact, being met in a timely manner, is questionable.

Poor record-keeping practices hamper the department's ability to assess developer compliance

Currently, the planning and permitting department's unilateral agreement records consist of hard copy files and electronic data stored in the department's POSSE program. As one department staff acknowledged, retrieving data on affordable housing projects requires research in both hard copy and electronic files, which can be a time-consuming process. For example, electronic documents filed in the department's POSSE system are difficult to retrieve because file names are not descriptive. The monitoring report for the Mililani Mauka project, Ordinance 89-123, dated April 26, 2006 has a file name, "89/Z-006." In generating this document, we initially requested a division administrator to provide us with a copy of a monitoring report for this project. The administrator logged onto the POSSE system and began opening files at random because files were not descriptive. Several files were opened

before the monitoring report was identified. While we commend the department for moving toward electronic records management, its document filing conventions make retrieving data on affordable housing requirements very cumbersome.

As noted previously in this report, we reviewed zone change files for 18 development projects with affordable housing conditions to assess whether those files contained adequate information to properly monitor affordable housing conditions. We found that hard copy zone change files for all 18 development projects were missing annual reports for years that a report should have been filed. In another example of poor record-keeping, we reviewed 18 development project files with affordable housing conditions, which included 26 separate unilateral agreement ordinances. We found that the department's zone change files lacked 12 of 26 ordinances. For the purposes of our review, we obtained copies of the 12 missing ordinances from the city clerk's office. We question the department's effectiveness in monitoring unilateral agreement requirements if the files do not contain copies of all the applicable agreements. While some of the missing ordinances were superseded by subsequent ordinances, files should contain all pertinent documents so that staff can appropriately evaluate the developer's requirements.

The department reports unverified and flawed data to the council and public

In its *Annual Report on the Status of Land Use on O'ahu, Fiscal Year 2005*, the department of planning and permitting began providing more detailed information about affordable housing units actually constructed under unilateral agreements. The report lists 46 projects on O'ahu with at least 25 units planned, which are covered under a unilateral agreement, as well as identifies affordable housing requirements and how developers plan to meet those requirements. The department emphasizes that information contained in the report is based on the *developers' own estimates and tentative timetables*. In addition, the department's annual survey of developers is supplemented by a check of city files, unilateral agreements, and other sources. We found little evidence that the department validates this information. A department staff person we interviewed acknowledged that the department's annual report data on the status of affordable housing is not accurate. The Planning and Policy Branch compiles affordable housing data, which is submitted by developers. Discrepancies are likely because the developers report what they believe is the status of their affordable housing obligations, but not necessarily what the planning and permitting

department has approved. Exhibit 2.1 lists the 25 residential projects the affordable housing requirement has already been satisfied. Exhibit 2.2 identifies the 21 residential projects with outstanding affordable housing requirements as of June 30, 2005.

Exhibit 2.1
List of Residential Projects That Met Affordable Housing Requirements as of June 30, 2005

<i>Project Name</i>	<i>Development Area</i>	<i>Total Housing Units At Project Buildout</i>	<i>No. Of Affordable Housing Required Under UA</i>	<i>No. Of Affordable Housing Units Built</i>	<i>Year Completed</i>	<i>Affordable Housing Requirement</i>	<i>In-lieu Fees Paid</i>
1. Ali'i Plantation	PUC	157	15	15	1984	10 percent	\$0
2. Crosspointe	PUC	546	55	55	1988	10 percent	\$0
3. The Crowne at Wailuna	PUC	158	16	0	1995	10 percent or in-lieu fee	\$1,120,000
4. Nahalekaha	PUC	29	3	3	1987	10 percent (off site)	\$0
5. Newtown Meadows	PUC	152	16	0	1987	10 percent or in-lieu fee	\$152,000
6. Pearl Horizons	PUC	222	23	0	1990	10 percent or in-lieu fee	\$400,000
7. College Gardens	Central	120	15	15	1984	10 percent plus 3 units	\$0
8. Kahi Kani	Central	344	344	344	1990	100 percent	\$0
9. Launani Valley	Central	833	128	128	2004	15 percent	\$0
10. Mililani Plantations	Central	2,150	215	215	1990	10 percent	\$0
11. Mililani Units 60/61/Ridge	Central	640	65	65	1991	10 percent	\$0
12. Waipi'o Unit 64	Central	46	23	23	1992	50 percent	\$0
13. Halekua Gardens *	Central	252	252	252	1994	50 percent plus off-site	\$0
14. Royal Kunia Phase I *	Central	1,627	1,365	1,365	2004	50 percent	\$0
15. Village Park (park site) *	Central	43	43	43	1988	10 percent	\$0
16. Waikele	Central	2,937	1,469	1,469	2002	50 percent	\$0
17. Waipahu Hall Elderly	Central	106	72	72	1985	50 percent	\$0
18. Waipi'o Gentry	Central	2,984	299	299	1985	10 percent	\$0
19. Kai Nui (Marina 4-B)	E. Honolulu	36	11	0	2001	30 percent or in-lieu fee	\$194,306
20. Hawai'i Kai Ret. Comm.	E. Honolulu	366	37	0	2001	10 percent or in-lieu fee	\$100,000
21. Kalama Ku'u	E. Honolulu	81	9	0	2003	10 percent or in-lieu fee	\$52,611
22. Leolani at Hawai'i Kai	E. Honolulu	60	0	0	2005	in-lieu fee or negotiated	\$258,000
23. Kailua Bluffs	Ko'olaupoko	329	39	39	2005	10 percent plus off-site	\$0
24. Pa'ala'a Kai	N. Shore	310	310	310	1981	100 percent	\$0
25. Ma'ili Kai, Phase IA	Wai'anae	85	58	58	1998	100 percent (27 off-site)	\$0
TOTAL		14,613	4,882	4,770			\$2,276,917

* Insufficient records to reconcile the affordable housing requirement with the actual number of affordable housing units built

Source: Annual Report on the Status of Land Use on O'ahu, Fiscal Year 2005

Exhibit 2.2

List of Residential Projects with Affordable Housing Requirements Outstanding as of June 30, 2005

<i>Project Name</i>	<i>Development Area</i>	<i>Estimated Total Housing Units at Project Buildout</i>	<i>Estimated No. of Affordable Housing Required Under UA</i>	<i>No. of Affordable Housing Units Built as of 6/30/05</i>	<i>Affordable Housing Requirement</i>	<i>In-lieu Fees Paid to Date</i>
1. Kapolei Knolls	Ewa	425	128	0	30 percent (off site)	\$0
2. Kapolei Senior Living	Ewa	650	0	0	Continuing care exception	\$0
3. Mehana at Kapolei	Ewa	1,150	345	0	30 percent	\$0
4. Kapolei Mixed Use	Ewa	300	90	0	30 percent	\$0
5. Kapolei Mauka	Ewa	750	250	0	Developer plan; no UA enacted	\$0
6. Ewa by Gentry	Ewa	7,163	2,781	2,329	10/30/60 percent for various areas	\$0
7. Ewa Makai by Gentry	Ewa	1,865	615	0	30 percent	\$0
8. Kapolei West (Ko Olina 2)	Ewa	2,370	500	0	Developer plan; no UA enacted	\$0
9. Ko Olina Resort	Ewa	4,450	392	392	10 percent of non-resort (off site)	\$0
10. Makaiwa Hills	Ewa	4,100	1,200	0	Developer plan; no UA enacted	\$0
11. Makakilo (1983 rezonings)	Ewa	1,842	355	355	10 percent plus 128 for other project	\$680,324*
12. Ocean Pointe	Ewa	4,850	821	821	10 or 30 percent (minus rental credits)	\$0
13. Villages of Kapolei	Ewa	4,280	1,909	1,909	30 percent	\$0
14. Mililani Mauka	Central	6,486	2,869	2,869	50/30 percent for various sites	\$0
15. Royal Kunia, Phase II	Central	2,000	600	0	30 percent	\$0
16. Waiawa by Gentry, I and II	Central	5,540	1,662	0	30 percent (less other credits)	\$0
17. Hawai'i Kai (various)	E. Honolulu	1,780	100	31	10 percent (100 units if built by 2005)	\$0
18. Bay View Estates**	Ko'olaupoko	27	6	6	30 percent provided off-site	\$0
19. Ma'ili Kai, Phase II	Wai'anae	853	318	100	30 percent	\$0
20. Makaha Valley Estates	Wai'anae	240	29	0	10 percent	\$0
21. Nanikeola Village	Wai'anae	144	41	0	30 percent (agreement pending)	\$0
TOTAL		51,265	15,011	8,812		\$680,324

* The Department of Budget and Fiscal Services can only verify \$133,371.

** The city and the Bayview Estates developer agreed upon an affordable housing requirement of six (6) units.

Source: *Annual Report on the Status of Land Use on O'ahu, Fiscal Year 2005*

In its 2005 annual report, the department indicated that as of June 30, 2005 the developer for the Ocean Pointe project, under Ordinances 85-44 and 93-44, had constructed 821 affordable units, which was its estimated requirement. However, we found a letter from the department to the developer dated October 13, 2004 which a planning division staff annotated a correction. We confirmed with the staff that the developer should have been credited with 788 units of its 771 unit requirement and not the 821 affordable units initially confirmed. While we acknowledge that the developer met its affordable housing requirement, the actual number of units reported overstated the developer's actual contribution by 33 units. This discrepancy was retained in the draft data to be included in the 2006 annual report, which affirms affordable housing data

as of June 30, 2006. The planning division staff person we interviewed confirmed that the annual report data for Ocean Pointe is incorrect. The department's poor record-keeping limits its ability to provide accurate, verified information. As a result, the council and public do not receive the true status of developers' compliance with affordable housing conditions and may be misled to believe that actual housing units were constructed. Furthermore, the council is left to make affordable housing-related decisions based on unverified, and potentially flawed, affordable housing data.

We also found that the department's 2005 annual report data underreports in-lieu fee collections by \$2,056,200. According to budget and fiscal services department data, the city collected in-lieu fees from the College Garden (\$21,200), Ali'i Plantation (\$35,000), and Ewa by Gentry (\$2,000,000) projects, totaling \$2,056,200. As Exhibits 2.1 and 2.2 indicate, none of these in-lieu fees were reported in the department of planning and permitting's 2005 annual report on the status of land use on O'ahu. Thus, the department seemed unaware of these payments and underreported in-lieu fee collections by over \$2 million. Due to poor record-keeping, we were unable to verify whether the developers delivered actual affordable housing units as indicated in the 2005 annual report data, or whether any units were replaced with in-lieu fees.

The department does not maintain historical affordable housing data

The City and County of Honolulu has been utilizing zone change conditions in unilateral agreements for affordable housing since the 1970s to help meet the city's affordable housing needs. A department of planning and permitting administrator estimates that since the city started using unilateral agreements in zone change ordinances, the city has created 13,000 for-sale and for-rent affordable housing units. However, we found that the department does not maintain an inventory of these housing units and cannot provide the basis for this figure. Thus, we are unable to verify this claim. A planning division administrator noted that applicable data is available, but that it would be a monumental task to inventory all affordable housing units. Although the division administrator acknowledged that an inventory of affordable housing units constructed under unilateral agreements may have value, the department does not have enough staff to compile such an inventory.

Inadequate staffing is blamed for poor monitoring

A planning division administrator notes that when the former department of housing and community development was eliminated in 1998, the department of planning and permitting assumed the responsibility for

monitoring unilateral agreements. The administrator emphasized that the department received no additional staff or funding to support this new responsibility. The lack of staff is cited by the planning division as the primary reason for poor unilateral agreement monitoring and record-keeping.

From 1999 to 2002, unilateral agreement monitoring was conducted by the department of planning and permitting's monitoring and compliance branch. At that time, the branch had five staff assigned to unilateral agreement monitoring. In 2002, unilateral agreement monitoring was transferred to the department's planning division. As of January 2007, the planning division allocated one full-time staff person to exclusively manage unilateral agreements in affordable housing. Two other staff persons provide part-time support for unilateral agreement monitoring activities. A former monitoring and compliance branch administrator we spoke with questioned whether one staff person was sufficient to effectively monitor unilateral agreements in affordable housing. A planning division administrator commented that the department needs an additional 1.5 full-time equivalent (FTE) employees to better manage unilateral agreements. Another division administrator estimates that the department could use two additional planners to effectively administer all unilateral agreements.

While we acknowledge that the planning and permitting department did not receive any additional staff or resources when it received responsibility for administering unilateral agreements, the department nevertheless has had this responsibility for nearly nine years. The department had ample opportunity to request needed resources or reallocate existing resources to effectively meet their mandate. We suggest that the department evaluate its staffing allocation for unilateral agreement monitoring and, if necessary, redistribute current staff or request the necessary number of positions necessary to fulfill its responsibilities in managing unilateral agreements.

In-lieu Fee Collections Have Not Resulted in Affordable Housing Benefits as Intended

In-lieu fee collections have not resulted in affordable housing benefits for the 80-120 percent of median income group. Since 1998, in-lieu fees collected from developers have not been expended for affordable housing-related purposes. The Housing Development Special Fund, which holds in-lieu fees, is not specifically intended for the development of affordable housing and limits the city's ability to expend in-lieu fees for affordable housing purposes. The acceptance of in-lieu fees, which

releases developers from constructing a required number of affordable homes within developments, may be inconsistent with current general, development, and sustainable community plans related to affordable housing.

Since 1998, no in-lieu fees were expended for affordable housing-related purposes

Current unilateral agreements and departmental rules afford developers the option of paying in-lieu fees to satisfy affordable housing requirements. In-lieu fees are cash contributions made by a housing developer to the city, to satisfy part or all of an affordable housing requirement established by unilateral agreement. The payment of an in-lieu fee has been offered via ordinance or by the department of planning and permitting and its predecessor department since 1983, as an alternative to actually constructing low- and moderate-income housing units. From the FY1992-93 to FY2005-06, the city has collected nearly \$4.5 million in in-lieu fee payments from developers for affordable housing requirements.

The in-lieu fees collected are deposited into the Housing Development Special Fund. The purpose of this special fund is to develop housing for sale or rental in the city and county of Honolulu. In 2004, the former Department of Budget and Fiscal Services director reported that the housing development special fund held \$391,371 of in-lieu fees. The director also noted that this amount was accumulating since 1998 and that none of the fees had been expended. Our review of in-lieu fee expenditures confirmed this assertion. We examined in-lieu fee expenditures for the period covering FY1991-92 through FY2005-06 and determined that there were no in-lieu fee expenditures during this entire period for any purpose, including affordable housing. The net effect of the current situation is that the city is accepting cash payments from developers instead of actual housing units built and that those monies are not spent on affordable housing-related initiatives.

The abolishment of the city's housing department and function in 1998 resulted in the awkward division of its functions among existing departments. In-lieu fees were still collected, but the lack of coordination between the departments of planning and permitting and budget and fiscal services, appears to have partially contributed to the lack of planning and control required for applying collected in-lieu fees towards affordable housing initiatives or purposes.

Exhibit 2.3 Photo of The Crowne at Wailuna



In 1995, the developers for The Crowne at Wailuna project in Aiea paid \$1,120,000 in in-lieu fees instead of constructing 16 affordable housing units as required by unilateral agreement. We found no evidence that the in-lieu fees collected were spent on affordable housing initiatives.

Source: Office of the City Auditor photo

There are no plans, goals, or objectives for spending in-lieu fees

In our review, we discovered several issues that contributed to the ineffectiveness of spending in-lieu fees for affordable housing purposes. They include the lack of coordination and planning by existing departments, special fund restrictions, transfer of previously collected in-lieu fees to the general fund, and in-lieu fee formula. However, a primary factor was that there were no plans, goals, or objectives for spending in-lieu fees collected from developers.

Although prescribed as an alternative for developers to satisfy all or part of their affordable housing requirements, there are no existing plans, goals, or objectives to guide the city's planning or fiscal departments on their expenditure, much less ensure that in-lieu fees are used to support affordable housing initiatives or purposes. We also note that neither

department has effective control to manage and plan the use of these fees. Although there are general, development, or community plans that have affordable housing policies and objectives, there is no effective coordination or direction to ensure that in-lieu fees are expended for these purposes.

Furthermore, in-lieu fees are deposited in a fund that does not prioritize their use for affordable housing initiatives or assistance purposes. In-lieu fees were previously deposited in the Housing Assistance Fund, which was abolished in 1998. A legal interpretation on the use of in-lieu fees suggested that the fees could be used for providing grant, credit, or cash subsidy to assist low income purchasers' qualification into the developments from which in-lieu fees were collected. For example, if an in-lieu fee is collected for Mililani Project A, then the collected fee should be spent to assist low- or moderate-income home buyers or renters in accessing housing units in Mililani Project A.

However, the in-lieu fees collected and deposited into the housing assistance fund were transferred into the general fund in 1998 after the abolishment of the Housing Assistance Fund that same year. After the housing assistance fund was eliminated, in-lieu fees were directed into the Housing Development Special Fund. This fund was set up for the development of housing for sale or rental, but its effectiveness in providing for affordable housing was initially diminished because it did not receive any of the in-lieu fees collected prior to 1998.

Lapsing the housing assistance fund into the general fund adversely impacted the housing development special fund's future effectiveness

In a memorandum dated January 13, 2004, in response to an inquiry relating to council resolution 03-265, the former budget and fiscal services director indicated that the housing development special fund held \$391,371 of in-lieu fees. The director commented that this total had been accumulating since 1998, and that none of the fees had been expended since that time. The director also noted that previously received in-lieu fees were placed in the housing assistance fund, which was abolished in 1998, and the contents of that fund were transferred to the city's general fund.

Our review of in-lieu fee expenditures confirmed that no in-lieu fees were expended from the housing development special fund from FY 1998-99 to FY 2005-06. We also examined the expenditure of in-lieu fees deposited into the housing assistance fund for the period covering

FY1991-92 through its abolishment in 1998 and found that there were no in-lieu fee expenditures from that fund since 1992. We found that substantial amounts of in-lieu fees collected prior to 1998 were redirected to the city's general fund, as a result of the abolishment of the housing assistance fund. Our review found that \$3,276,200 of in-lieu fees for affordable housing requirements were lapsed into the city's general fund.

This was not the only instance of in-lieu fees being deposited to the general fund rather than being retained for affordable housing assistance or development purposes. In FY2000-01 and FY2001-02, we found that an additional \$246,917 of in-lieu fees for two separate housing projects were deposited into the city's general fund rather than the housing development special fund as required by law.

In total, we found that at least \$3,523,117 in in-lieu fees was redirected to the general fund during our review period of FY1992-93 to FY2005-06. The amount redirected to the general fund is likely larger than this, as the period of review did not include any FY1987-88 to FY1991-92 in-lieu fee collections, which were also unexpended for housing assistance and lapsed to the general fund.

The budget and fiscal services department identified in-lieu fees totaling \$4,461,440 collected between FY1992-93 and FY2005-06. Of this amount, \$3,523,117 was redirected to the city's general fund. This substantial transfer of in-lieu fees to the general fund adversely impacted the housing development special fund's future effectiveness. Exhibit 2.4 displays in-lieu fee collections from FY1992-93 to FY2005-06.

**Exhibit 2.4
In-lieu Fee Collections, FY1992-93 through FY2005-06**

<i>Fiscal Year</i>	<i>Project Name</i>	<i>Geographic Area</i>	<i>Developer</i>	<i>Affordable Units Required as of 6/30/05</i>	<i>In-Lieu Fee Paid</i>	<i>Disposition</i>
FY1992-93	College Gardens	Central Oahu (Waiawa)	Pearl Harbor Heights Developer (PHH)	15	\$10,600	Housing Assistance Fund (HAF)
FY1992-93	Ewa by Gentry	Ewa	Gentry-Pacific	Unknown	\$2,000,000*	HAF
FY1992-93	Ali'i Plantations	Primary Urban Center (Halawa)	Lear-Sigler (LSI)	15	\$14,000	HAF
FY1993-94	Ali'i Plantations	Primary Urban Center (Halawa)	LSI	---	\$7,000	HAF
FY1993-94	College Gardens	Central Oahu (Waiawa)	PHH	---	\$10,600	HAF
FY1994-95	Wailuna IV	Primary Urban Center (Aiea)	Lusk	16	\$1,120,000	HAF
FY1995-96	Ali'i Plantations	Primary Urban Center (Halawa)	LSI	---	\$14,000	HAF
FY1996-97**	Elderly Care Facilities	E. Honolulu	Kaiser Development	37	\$100,000	HAF
FY2000-01	Keahole Street Marina 4B	E. Honolulu (Hawai'i Kai)	Schuler Homes	10	\$194,306	General Fund (GF)
FY2001-02	Kalama Valley	E. Honolulu (Hawai'i Kai)	Schuler Homes	10	\$52,611	GF***
FY2002-03	Le'olani (Kamilonui)	E. Honolulu (Hawai'i Kai)	Schuler Homes	18	\$258,000	Housing Development Special Fund (HDSF)
FY2003-04	Seascape	Ewa (Makakilo)	Schuler Homes	9	\$133,371	HDSF
FY2004-05	Palehua East B Makakilo	Ewa (Makakilo)	Castle & Cooke	28	\$428,400	HDSF
FY2004-05	Makakilo	Ewa (Makakilo)	D. R. Horton Schuler	8	\$118,552****	Collected, But Later Returned to Developer
Totals				166	\$4,461,440	

* Unilateral agreement file and DPP's 2005 annual report do not indicate a \$2 million in-lieu fee payment.

** No in-lieu fees were reported as collected during FY1997-98 through FY1999-2000, and FY2005-06.

*** BFS directed these in-lieu fees into the General Fund instead of the Housing Development Special Fund.

**** DPP records indicate that these in-lieu fees were returned to the developer.

Source: Department of Budget and Fiscal Services and Department of Planning and Permitting

We also identified a discrepancy in the budget and fiscal service department's accounting of in-lieu fee collections. We found a letter from the planning and permitting department dated June 22, 2004, indicating that it had returned checks to Schuler Homes totaling \$118,498 for in-lieu fees paid on its Makakilo project. However, the budget and fiscal services department maintains that it deposited the same amount in in-lieu fees into the housing development special fund in FY2004-05. We emphasize that planning and permitting returned the developer's checks; it did not issue a refund from the city's treasury. Thus, we question how budget and fiscal services could have posted the in-lieu fee collection if the checks were returned to the developer.

Because the purpose of the housing development special fund is to develop housing for sale or rent, lapses into the general fund significantly impacted the city's ability to effectively use in-lieu fees for development of affordable housing units for sale or rent. Additionally, the housing development special fund, where in-lieu fees are deposited, does not specify the development of affordable units. Thus, the in-lieu fees deposited are not required to be used for affordable housing purposes.

The housing development special fund is not specifically intended for the development of affordable housing

The in-lieu fees collected from developers to satisfy all or part of their affordable housing requirements are deposited in the housing development special fund. The purpose of the fund is the development of housing for sale or rental in the city and county of Honolulu with no specific reference to *affordable* housing. There is no provision that in-lieu fees collected from developers be used for affordable housing development; and no guidance on how these fees should be expended.

Under the current system, the city cannot be assured that in-lieu fees will be used for affordable housing purposes due to the fund's broad purpose, and lack of guidance on how in-lieu fees should be collected and expended. Moreover, because there is no specific city agency tasked with monitoring, planning, or expending in-lieu fees collected from developers, these funds are subject to use for general housing purposes.

The city cannot be assured that in-lieu fees will be used for affordable housing purposes

The housing development special fund consists primarily of monies authorized by council appropriations and is used as a pass-through for various city development and revitalization projects. In-lieu fees represent a relatively small proportion of the fund. Because there is no provision to treat in-lieu fees separately, in-lieu fees could be used to

supplement the fund's primary uses such as capital improvement project funding or other related expenses. Although no in-lieu fees were ultimately expended, the purpose of this fund does not ensure that the city will receive *affordable* housing benefits.

No specific city agency is tasked to monitor, plan, or expend in-lieu fees collected from developers

Since the abolishment of the city's housing department by the city-wide reorganization in 1998, there is no specific city agency tasked to monitor, plan, or expend the in-lieu fees collected from developers, or housing development special fund monies. Various housing functions are scattered between the departments of planning and permitting and budget and fiscal services, and do not appear to be effectively coordinated to substitute for the lack of a housing agency. Moreover, there is no department tasked with ensuring in-lieu fees collected from developers are applied towards affordable housing initiatives.

Currently, the department of budget and fiscal services is responsible for administering the housing development special fund, including accounting for the collection and disbursement of in-lieu fees collected from developers. However, it does not determine the amount of these fees, plan the use of collected fees, or determine affordable housing priorities.

We found that the Department of Design and Construction has expended the majority of housing development special fund money since the dissolution of the former Department of Housing and Community Development, which were earmarked for capital improvement projects and related priorities. In-lieu fees are deposited into the housing development special fund, but the department expended none during our review period. We found that the department's role is limited to implementing the housing development priorities established by the city administration or city council, but appears to have no role in developing affordable housing development priorities. Although the department of planning and permitting approves the content of unilateral agreements, including the substitution of in-lieu fees to settle a developer's obligation to build affordable housing, and monitors the implementation of the terms of unilateral agreements, it does not ensure that the in-lieu fees collected from developers are expended on affordable housing initiatives, nor plan the use of the fees negotiated from developers.

We did not find any coordinated activity among the departments to monitor, plan, or expend the in-lieu fees collected from developers to ensure their use for affordable housing purposes. As a result, in-lieu fees

are not being expended for affordable housing purposes. Furthermore, we found that the lack of coordination among departments may have contributed to housing development special fund expenditures on purposes entirely unrelated to housing development.

In-lieu fees may have been expended for purposes other than housing

While examining the disbursement of in-lieu fees from the housing development special fund, we found instances where money from the special fund was being used for purposes other than the development of housing for sale or rental in the city and county of Honolulu. The lack of monitoring, control or coordination between city agencies regarding the use of this fund may have prompted instances of improper fund use. Since housing development special fund expenditures for capital improvement projects was outside the scope of this audit, we did not conduct a full assessment of these expenditures.

We specifically found that post-1998, or after the abolishment of the housing department, housing development special fund monies amounting to more than \$366,000 were used for purposes other than development of housing units for sale or rental including: commercial relocation expenses; commercial property management expenses; and commercial storage expenses. These, and other questionable expenditures, are identified in Exhibit 2.5. Certain expenditures were not related to housing development, which is the fund's primary purpose. The lack of monitoring, control or coordination among existing departments failed to ensure that the purposes of the housing development special fund are achieved.

**Exhibit 2.5
Non-housing Development Related Expenditures of Housing
Development Special Funds After FY1997-98**

<i>Fiscal Year</i>	<i>Project Name</i>	<i>Purpose</i>	<i>Amount Expended</i>
FY2001-02	Ewa Mill Relocation	Business relocation	\$315,000
FY2002-03	Ewa Mill Relocation	Miscellaneous relocation expenses	\$848
FY2004-05	Ewa Villages	Property management	\$24,116
FY2005-06	Ewa Villages	Property management	\$24,990
FY2005-06	Ewa Mill Relocation	Storage fees	\$1,143
Total Expended			\$366,097

Source: Department of Budget and Fiscal Services

The current framework for the collection of in-lieu fees is inadequate for significant development of affordable housing or rentals

Since 1998, in-lieu fees have not been expended for affordable housing-related purposes. The current housing development special fund balance of in-lieu fees is approximately \$820,000. Given current restrictions on the use of the fund, the total value of in-lieu fees would be insufficient for developing housing for sale or rent.

Previous *ad hoc* in-lieu fee assessments in unilateral agreements as well as the current in-lieu fee formula contained in the rules for unilateral agreements with affordable housing do not result in significant in-lieu fee collections. The current formula only results in a nominal fee, as compared to the cost/value of a constructed affordable unit. Hawai'i county increased its in-lieu fee formula to promote construction of required affordable homes after experiencing similar problems with collecting nominal in-lieu fees.

Zoning changes are to be considered in light of general and development plan objectives and policies, which include affordable housing objectives. However, in-lieu fees have not been spent to benefit the low- and moderate-income community in which the unilateral agreement is

imposed. Some development projects have met their entire affordable housing requirements without constructing any affordable housing units.

Current fund balance cannot develop a significant amount of affordable housing for sale or rent

The current in-lieu fee balance is approximately \$820,000. The in-lieu fees are deposited into the housing development special fund, and are subject to the fund's purpose of developing housing for sale or rental in the county. Although developers paid cash instead of actually constructing housing units for all or a portion of their affordable housing requirement, there is nothing in the fund's requirements (or other legal requirements) mandating that the in-lieu fees be used to only develop *affordable* housing or rentals.

The term *develop* in Section 6-46.2, ROH, limits the potential use of the in-lieu fees in the fund. Housing development requires significant resources, as opposed to subsidies, grants, or alternative uses which could be applied to affordable housing initiatives in smaller amounts over time. Given the current balance of the total in-lieu fees and the housing development special fund's broader purpose, the city may only be able to develop housing for sale or rent on a nominal basis, which may not be the best use of the available funds.

The formula contained in the rules for unilateral agreements in affordable housing does not result in significant in-lieu fee collections. The current formula, which establishes the in-lieu fee as equal to the difference between the estimated costs of building the affordable housing units less the estimated sales price of the units, only results in a marginal fee compared with estimated affordable unit development costs. Unilateral agreements and their associated rules allow developers the option to satisfy part or all of their affordable housing requirements with a cash payment subject to the planning and permitting department's approval. The nominal nature of in-lieu fees have resulted in some development projects meeting their entire affordable housing requirements without constructing any affordable housing units.

Communities affected by zoning changes do not directly benefit from in-lieu fee collections

Since 1992, in-lieu fees have not been spent to benefit the community in which the unilateral agreement is imposed. A 1986 corporation counsel opinion advised the former department of housing and community development that in-lieu fees could be expended to address low- and

moderate-income housing needs in the project area affected by the unilateral agreement. The opinion suggested that in-lieu fees may also be used as a source to provide grant, credit or cash subsidy to assist low-income purchasers' qualification to purchase units within the development from which the in-lieu fees were collected. Corporation counsel's guidance established that in-lieu fees are intended to be spent on affordable housing purposes. We found, however, that some development projects have met their entire affordable housing requirement through in-lieu fees, but these fees were not spent for affordable housing purposes. Thus, those communities received no affordable housing benefit as intended.

Hawai'i county amended its in-lieu fee program due to the lack of affordable housing units built

In 2005, Hawai'i county amended its housing code to provide enhanced affordable housing development requirements and increased in-lieu fees. The county's housing administration found that developers differed in their desire to build affordable housing as part of their planned developments. Previous to the amendment, the county's affordable housing development requirement was to construct 10 percent affordable units development-wide or a pay an in-lieu fee of \$4,720 per required affordable unit. The result was that the fee was so nominal that developers found it more cost effective to pay the fee rather than building any required affordable housing units, creating a situation where no affordable housing units were constructed within developments.

The county changed its in-lieu fee formula to 25 percent of the difference between the fair market price and the 140 percent affordable median price. With the new formula, for example, a new market priced home may sell for \$750,000. The 140 percent median price for an affordable unit is \$290,000. The new formula would require an in-lieu fee of \$115,000 per unit. With the changes to the in-lieu fee formula, Hawai'i County housing administration noted that developers have to carefully consider whether they want to pay in-lieu fees or construct affordable housing units.

The county indicated that since the fee formula change, developers are now choosing to build actual housing units to satisfy their affordable housing requirements; and no in-lieu fees were collected in the past two years.

The acceptance of in-lieu fees may be inconsistent with current general, development, and sustainable community plans related to the construction of affordable housing units

In-lieu fees collected from developers are not spent towards the achievement of general plan objectives and policies, or development and sustainable community plans regarding affordable housing opportunities. Current restrictions on the use of in-lieu fees do not support policy objectives regarding the development of affordable housing or providing a wide range of income-based housing opportunities. Acceptance of in-lieu fees may be inconsistent with current development and sustainable community plans, which have a preference for creating affordable housing purchase or rental opportunities.

As discussed previously, there were no expenditures of in-lieu fees collected from developers. As such, none of the affordable housing purposes of the general plan, development plan, or sustainable communities plans regarding affordable housing were supported or advanced by the expenditure of in-lieu fees.

Compliance with general, development, and sustainable communities plans related to affordable housing is not documented

While the department of planning and permitting issues an annual report on O‘ahu’s land use, it does not report or document general, development, or sustainable community plan compliance in its unilateral agreement options in affordable housing. The department also does not document or require developers to justify how developer delivery options, including in-lieu fees, are consistent with general, development, or sustainable community plans.

Currently, the city allows developers to forgo affordable housing construction in-lieu of cash payments, despite an expressed desire for more affordable housing opportunities as stated in the general, development, and sustainable community plans. In at least seven instances developers were allowed to develop residential projects without constructing any affordable housing units, despite an affordable housing requirement. Moreover, the city has not expended any of the resulting in-lieu fees collected on affordable housing initiatives or purposes. The city cannot be assured that the various delivery options authorized by the department of planning and permitting, particularly its acceptance of in-lieu fees, are consistent with general, development, and sustainable community plans, which promote affordable housing options.

Limitations on use of in-lieu fees do not support the city's plans

As noted previously, in-lieu fees are restricted by the purpose of the housing development special fund, and may only be used only to develop housing for sale or rental in the city and county of Honolulu. There is no requirement that the housing developed be affordable, even though the fee money collected from the developer is meant to compensate the city for not constructing affordable housing units. The estimated total of in-lieu fees collected and deposited in the housing development special fund practicably cannot develop a significant amount of housing for sale or rent. The term *develop* severely limits the potential use of in-lieu fees collected. Thus, the city cannot be assured that in-lieu fees are spent on affordable housing initiatives, which are expressed in the general, development, and sustainable communities plans.

For example, General Plan Housing Objective A is to provide decent housing for all the people of O'ahu at prices they can afford. However, the city no longer directly develops affordable housing nor has a housing specific function. As such, the city's involvement in providing decent housing at affordable prices to O'ahu residents is largely confined to its power to impose affordable housing conditions via unilateral agreements.

The acceptance of in-lieu fees as a delivery option to fulfill part or all of a developer's affordable housing requirements makes it more difficult for the city to achieve this objective because:

- the city no longer directly develops housing;
- the city's use of the fees is restricted to only developing housing for sale or rent;
- the amount of typical in-lieu fees collected are nominal in comparison to potential development costs; and
- the amount of total in-lieu fees collected, if not geographically restricted, will not result in significant development of affordable housing for sale or rent in the affected area.

Since the city also accepts cash payments to fulfill all or part of affordable housing requirements imposed on developers, the city may consider alternative ways to support the general plan's housing objective by including options such as:

- eliminating/discouraging the collection of in-lieu fees;
- raising the in-lieu fee formula to induce actual development of affordable housing;
- determining the housing or development purposes for which in-lieu fees may be properly used (e.g., planning seed money, grants to non-profits, affordable rent subsidy, etc.); or
- further restricting the use of in-lieu fees collected to affordable housing purposes only, or to specific affordable housing objectives in a given community.

As part of the General Plan, Housing Objective C, policies include:

- encourage residential developments that offer a variety of homes to people of different income levels and to families of various sizes, and
- encourage the fair distribution of low- and moderate-income housing throughout the island.

If the city accepts in-lieu fees rather than requiring developers to construct actual affordable housing units in areas where the distribution of low- and moderate-income housing is desirable or needed, or where an area's housing could be more diverse and inclusionary of varying income levels, it amounts to a failure of implementing these policies. Current special fund restrictions on the use of in-lieu fees artificially limit the city's ability to use a portion of these fees to creatively encourage and facilitate third party affordable housing development, rather than develop actual housing.

Lastly, each community has different development priorities and different needs regarding affordable housing, as expressed by development and sustainable community plans. Staying within the current framework, more attention is needed to make the critical policy decision on whether the collection of in-lieu fees should continue if they are not being spent. If the creation of more affordable housing is desired by a community plan, then actual housing construction is the preferred option, rather than accepting in-lieu fees. Moreover, none of these plans' affordable housing objectives are being supported by the housing development special fund's current restriction that the in-lieu fee money should be

used only for development. If in-lieu fees continue as a delivery option, amended rules or ordinances should be used to establish appropriate use of the fees.

The Department of Planning and Permitting's Authorization and Application of Excess Affordable Housing Credits Lack Accountability

As noted in chapter one of this report, developers have the option to construct affordable housing units for sale or rent to meet their affordable housing requirement. If they opt to construct housing units, developers will apply for housing credits, which are approved by the planning and permitting department and then credited against a developer's affordable housing requirement. Sometimes, developers will accrue affordable housing credits that exceed their minimum requirement, which become "excess" credits.

In practice, the planning and permitting department allows developers to apply these excess credits toward future affordable housing requirements, with some limitations. Hawai'i and Maui counties also allow developers to utilize excess credits for future projects, which are set forth in their respective county codes. However, we found that the city's program for accumulating and redeeming affordable housing credits is not formalized in ordinance or rule. The department of planning and permitting authorized developers to accumulate affordable housing credits contrary to city ordinance under a moratorium on affordable housing conditions. The department's excess affordable housing credit application practices are generally consistent with general, development, and sustainable communities plans related to affordable housing, but may conflict with the general plan's housing objective advocating diverse communities.

Accumulating and redeeming excess affordable housing credits are not formalized in ordinance or rule

The department's rules related to unilateral agreements in affordable housing provide developers with six delivery options in meeting its affordable housing requirement: 1) construct for-sale housing units; 2) construct rental housing units; 3) provide land to the city for affordable housing construction; 4) construct for-sale or for-rental affordable housing units off-site from the project; 5) provide a cash contribution, or in-lieu fee; and 6) provide finished house lots for affordable housing owner-builder efforts. In addition, the department of planning and permitting allows developers to apply excess housing credits to satisfy affordable housing requirements. This practice is not authorized by rule or ordinance, nor does the department formally track the balance, sale, or redemption of these credits.

The department maintains “practices” in managing excess affordable housing credits

If a developer chooses to construct affordable housing units to meet its affordable housing requirement, credits are granted based on the number of units built and, if applicable, the type of units built as referenced in Exhibit 1.2. In order for the developer to receive a credit, the for-sale housing unit must be owner-occupied by a qualified buyer for at least one year and for-rent units must be rented to a qualifying tenant for 10 years.

As an incentive for developers to construct more affordable housing units, the department of planning and permitting authorizes developers to continue earning housing credits in a project development, even if the minimum number of affordable housing units under the unilateral agreement has been met. A developer can then apply these excess credits toward an affordable housing obligation established under a separate unilateral agreement. The department of planning and permitting, however, does not maintain any formal, written policies or procedures regarding the accrual, application, or transfer of affordable housing credits, nor are provisions established in city ordinance.

In *practice*, the department’s unwritten policy generally allows developers to apply excess credits if:

- the credit earned is applied within the same development plan district;
- the credit earned is applied within a 7.5 mile radius from the project area where the credit was earned; and
- no more than 50 percent of the affordable housing requirement is satisfied with the use of excess credits.

In order to obtain authorization to use excess affordable housing credits, the developer must submit a letter to determine if the department is open to the “concept” of utilizing credits to fulfill a portion of the project’s affordable housing requirement. The department will review the developer’s request and respond. If the department indicates its preliminary acceptance of the proposed use of credits, the developer will then submit a formal request for using excess affordable housing credits by detailing the number of credits to be redeemed and the location for

their application. The planning and permitting department will then approve or deny the developer's application.

We interviewed representatives from three development companies that constructed affordable housing units under unilateral agreements. One of the developers was completely unaware of the department's practices regarding excess affordable housing credits. Another developer, who actively earned, banked, and proposed the use of excess credits, was unaware of the department's 7.5-mile radius rule. The planning and permitting department's effectiveness in managing the excess affordable housing credits is compromised if developers that claim to use such credits are not aware of the limitations on their use.

Affordable housing credits are not tracked to determine a developer's balance, sale, or redemption of excess affordable housing credits

Although the department recognizes excess credits and their potential impact on housing policy, a planning division administrator advised us that the department does not formally track developers' accrual, balance or sale of affordable housing credits. Rather, the department relies on developer-reported information. Another division administrator noted that at least three developers have used excess credits. One developer we spoke with estimates that it maintains 600 affordable housing credits that it can use toward future affordable housing requirements under unilateral agreements. Another developer claims to have 90 affordable housing credits. However, as noted previously in this report, the department does not maintain adequate records and is unable to confirm the total number of credits currently held by developers.

In addition to accruing and banking affordable housing credits, developers may also transfer or sell these credits. One developer we spoke with acknowledged purchasing affordable housing credits from another developer for a Makakilo housing project, but declined to disclose the amount paid for these credits because they were bundled with other development site assets. The developer representative further explained that developers negotiate for the sale of credits and that disclosing such information could compromise future sales. The two other developers we spoke with were unaware of the practice of affordable housing credit sales between developers. The department of planning and permitting does not have any rules or guidelines regarding the sale or transfer of affordable housing credits and takes the position that such transactions are a private business matter between developers. The department's only concern is that the credit earned is applied in

accordance with departmental practices governing the application of credits. In other words, the developer redeeming the credit is not as important as where that credit was earned and where it is being applied.

We identified only one instance where the council recognized and authorized the use of excess credits. In 2004, the council adopted Ordinance 04-08, which rezoned land in the Ewa district from agriculture to residential. In this ordinance, the council specifically authorized the developer to utilize affordable housing units from another project that were not needed to meet its affordable housing requirement. The developer's proposed affordable housing program estimated an affordable housing requirement of 555 units. Pursuant to the unilateral agreement, the developer pledged a total of 272 of the 426 excess credits the developer had banked to meet the affordable housing requirement under Ordinance 04-08. The developer pledged to construct the remaining 283 units to satisfy its affordable housing requirement. Unless the council intends to address the use of excess credits in every unilateral agreement with affordable housing, the department should formalize the credit application system. This will benefit the council, developers, and the public by providing a consistent means to accrue, bank, and apply these credits.

Exhibit 2.6
Photo of the Ewa by Gentry Project



A total of 272 excess affordable housing credits earned in the Ewa by Gentry project under Ordinances 91-17, 94-57 and 98-44 are being applied to the affordable housing requirement in the Ewa Makai by Gentry project under Ordinance 04-08.

Source: Office of the City Auditor photo

Hawai‘i and Maui counties codify credit use

Both Hawai‘i and Maui counties have codified the use of affordable housing credits. Hawai‘i county allows developers to apply excess affordable housing credits toward affordable housing requirements, which is codified in Section 11-15, Hawai‘i County Code. The county allows developers to use excess credits to fulfill all or part of an affordable housing requirement within a 15-mile radius from the project site where the credit was earned. Maui County authorizes the use of excess credits, but limits the application to the same community plan area in which the credit was earned and the credit must be applied toward the same type of unit constructed. The credit must also be used for the same income group in which the credit was earned. Provisions for the use of housing credits on Maui are codified in Chapter 2.96 of the county code. Kaua‘i county does not currently permit the use of excess affordable housing credits.

While we recognize the department's efforts to provide developer incentives to construct additional affordable housing units through the use of excess housing credits, we are concerned about the lack of accountability associated with the department's current practices. The use of excess affordable housing credits can have a significant impact on the number of affordable housing units actually constructed and influence housing policy. For example, if the council approves a unilateral agreement with an affordable housing requirement, this establishes a certain expectation that actual housing units will be constructed or that the city will receive an alternative affordable housing benefit. However, with the application of excess housing credits, up to one-half of the anticipated number of affordable housing units expected, or its commensurate benefit, may not materialize. We understand that affordable housing units were actually constructed in order to earn an excess housing credit. Nevertheless, the banking of these credits can have a significant impact on the affordable housing units constructed in the future. For example, if a developer built affordable housing in the Ewa development district in 1995, and received a credit for that unit in 1996, the credit would have been banked if it was not needed to fulfill the minimum obligation for that housing project. Consequently, in 2010, the council approves a zone change in the Ewa district, authorizing the developer to construct a new residential project, and initiates a unilateral agreement with an affordable housing requirement. In this instance, the developer could utilize the credit earned in 1996 to fulfill up to one-half of its affordable housing requirement, thereby significantly reducing the number of actual affordable housing units built and diminishing the anticipated inventory of affordable homes available to qualifying families in 2010 and beyond.

The lack of formal, written policies and procedures regarding the accrual, banking, and redeeming of excess credits may give the appearance that the department is arbitrary in its decisions. Council action notwithstanding, the planning and permitting department currently has wide discretion in authorizing the accumulation and use of credits and there is nothing to bind future department administrators from amending the current "practices" since they are not formalized in rule or ordinance. If the department were to formally establish their practices via departmental rules, the council, developers, and the public could provide input on this important affordable housing option.

The department authorized developers to accumulate excess affordable housing credits contrary to city ordinance under a moratorium on affordable housing conditions

In 1999, the city council adopted an ordinance that relaxed some of the affordable housing conditions in response to developers that were having difficulty selling affordable homes mandated under unilateral agreements. Although the ordinance was clearly intended to allow developers to meet their minimum obligations only, the planning and permitting department did not adhere to that intent and allowed some developers to bank a high number of affordable housing credits. The redemption of these credits may be contrary to housing objectives.

Ordinance 99-51 provided relief to developers during the market downturn

In August 1999, the city council adopted Ordinance 99-51, which temporarily amended the affordable housing conditions in unilateral agreements to permit the sale of affordable housing units free from any conditions related to buyer eligibility and restrictions on transfer. Under this ordinance, developers would remain obligated to deliver the numbers and types of affordable housing units at affordable prices required by unilateral agreement, but they could offer those units for sale to the general public without any buyback or shared appreciation conditions. The moratorium on affordable housing conditions was effective from August 1999 to August 2001. In June 2001, the council extended the moratorium until August 2005 by adopting Ordinance 01-33.

When the city council approved and extended the moratorium, it found that the real estate market on O‘ahu had undergone significant change. In connection with the general downturn in the state’s economy, the market had declined and real estate prices had fallen significantly, such that market prices were at or below the prices established for affordable housing units. As a result, developers were unable to sell affordable units required by unilateral agreement because buyers were opting to purchase market-priced units that were not subject to the restrictions on transfer associated with the affordable units. Restricting affordable home sales to buyers in specific income categories also reduced the potential number of buyers for the affordable units. Due to the depressed real estate market at the time, the affordable housing conditions established under unilateral agreements were not providing affordable housing units that were saleable and adversely impacted the housing and construction industries without any corresponding benefit to the public.

Section 3 (a)(2) of Ordinance 99-51 states, “the declarant shall receive full credit for any affordable housing units sold under this amendment, toward the number of affordable housing units required by the unilateral

agreement.” In our view, the council clearly established its intent that the moratorium would apply only to those affordable housing units needed to satisfy the developer’s requirement under unilateral agreements. We found, however, that the department of planning and permitting granted affordable housing credits in excess of the minimum number required under unilateral agreements. In fact, the department disclosed its authorization in allowing developers to stockpile affordable housing unit credits in its *Report on the Implementation of Ordinance 99-51*, dated February 6, 2001.

According to two planning division administrators, the department of planning and permitting granted affordable housing credits during the moratorium period of August 1999 to August 2005 as long as the developer complied with the criteria established for earning the credit. As a result, the department allowed some developers to gain undue benefit during the moratorium period by allowing them to accrue, and bank, affordable housing credits in excess of the minimum required under Ordinance 99-51.

Developers were able to bank affordable housing credits in excess of minimum requirements

Although planning division administrators are unable to determine the number of excess credits earned by developers, they acknowledge that since the moratorium was imposed, developers have been relying on credits to fulfill affordable housing conditions. Instead of meeting the minimum 30 percent requirement, some developers took advantage of market conditions during the moratorium and built 40-50 percent affordable units, thus banking credits for future use. Administrators estimate that at least three developers have claimed excess affordable housing credits during the moratorium.

One of the three developers we spoke with confirmed that they earned excess affordable housing credits during the moratorium, but this developer was unable to identify the number of excess credits earned. In reviewing developer records, we found that just prior to the moratorium, this developer had an outstanding affordable housing requirement of 178 credits in the low-income (below 80 percent median income) category; 465 credits in the moderate-income category (higher than 80 percent, but lower than 120 percent median income); and 176 credits in the above 120 percent, but lower than 140 percent median income category, for a total of 819 credits. Although departmental rules do not contain an affordable housing requirement for income levels that exceed 120 percent of median income, in this example, the city council

established a third tier in the developer's affordable housing requirement targeting the over 120 percent, but not more than 140 percent median household income group. From August 6, 1999 to June 30, 2005, the department of planning and permitting granted the developer 572 credits in the 80-120 percent category; 549 credits in the 120 – 140 percent category; and one credit in the 140 percent category, for a total of 1,122 credits. Exhibit 2.7 details this developer's affordable housing requirement and the number of credits earned during the moratorium. Ordinance 99-51 cited market conditions where comparable market units were priced at or below affordable housing units with unilateral agreement-imposed conditions. By not limiting the application of credits to a developer's minimum requirement only, the department of planning and permitting allowed this developer to obtain an affordable housing credit for market-priced units.

Exhibit 2.7

Example of a Developer's Accrual of Excess Affordable Housing Credits During the Moratorium Under Ordinances 99-51 and 01-33

	<80%	80% to <120%	120% to <140%	Total
Total affordable housing requirement	686	1092	470	2,248
Credits approved prior to moratorium	478	150	102	730
Units sold prior to 8/5/99	30	477	192	699
Total potential credits received prior to moratorium	508	627	294	1,429
Total outstanding affordable housing requirement prior to the moratorium	178	465	176	819
Units closed 8/6/99 to 12/31/99	51	47	0	98
Units closed 1/1/00 to 6/31/00	33	58	0	91
Units closed 7/1/00 to 12/31/00	42	68	0	110
Units closed 1/1/01 to 6/30/01	68	6	0	74
Units closed 7/1/01 to 12/31/01	79	36	1	116
Units closed 1/1/02 to 6/30/02	73	36	0	109
Units closed 7/1/02 to 12/31/02	72	84	0	156
Units closed 1/1/03 to 6/30/03	86	84	0	170
Units closed 7/1/03 to 12/31/03	52	104	0	156
Units closed 1/1/04 to 6/30/04*	16	26	0	42
Units closed 7/1/04 to 12/31/04*	0	0	0	0
Units closed 1/1/05 to 6/30/05*	0	0	0	0
Total AH credits earned and approved during moratorium	572	549	1	1,122
Potential excess credits as of 6/30/05	394	84	0	303

* Additional affordable housing units closed but the developer had not yet received credit. It is possible that additional credits were earned, but not properly recorded.

Source: Office of the City Auditor based on developer-reported data

Redemption of excess credits earned during the moratorium may conflict with the intent of the city's affordable housing program

Ordinance 99-51 eliminated the requirements for restrictions on buyer eligibility and transfer of ownership in the future. It also reduced some of the filing requirements for developers, such as the need to provide buyer's tax returns. In addition, the buyback and shared appreciation provisions were reduced from ten years to three years for existing owners of affordable housing units. In its *Report on Affordable Units and Buyers Under Ordinance 01-33*, February 28, 2005, the planning and permitting department disclosed that between 2001 and 2005, their analysis indicated that only 30 percent of the affordable housing units were purchased by families whose incomes would have met the low- or moderate-income limits in place before the moratorium established under Ordinance 99-51. The department also found that incomes of half of the purchasing households were equal to or greater than 20 percent above the maximum income limits, and a quarter of the households had incomes equal or greater than 49 percent above the limits. Thus, developers received affordable housing credits for future use that were earned by selling housing units to families and individuals who would not have otherwise qualified for affordable housing.

In addition, we question whether authorizing developers to apply affordable housing credits earned during the moratorium toward future affordable housing requirements is in keeping with the intent of the city's affordable housing program. Since the moratorium under Ordinance 99-51 has been lifted, developers must once again comply with affordable housing conditions, which include qualifying buyers by income, and attaching resale conditions to affordable units. However, the credits earned during the moratorium were not subject to these same restrictions. Thus, developers are able to forgo constructing an actual affordable housing unit in the future, with restrictions, and replace that requirement with a credit that may have been earned without restrictions.

The department's excess affordable housing credit practices may conflict with the general plan's housing objective advocating diverse communities

The general, development, and sustainable communities plans all express a desire for some form of affordable housing. The general plan encourages residential developments that offer a variety of homes to people of different income levels and to families of various sizes. The department's practices in authorizing excess affordable housing credits generally conform to the plans' tenets, with the exception of diverse communities.

Incentives to construct more affordable housing units are consistent with general, development, and sustainable communities plan provisions in affordable housing

The planning and permitting department's current policy allows developers to earn excess affordable housing credits and apply them to satisfy no more than 50 percent of an affordable housing requirement as long as the credit is used within a development plan district and a 7.5-mile radius between projects. Allowing the use of credits provides an incentive for developers to construct more affordable housing units. In addition, the rules for unilateral agreements in affordable housing allow developers to earn enhanced credits for building larger units. As a result of the informal credit system, developers are encouraged to build more affordable housing units, and larger units, which benefit a greater number of qualified individuals and families. Additionally, an actual affordable housing unit constructed in the present has a higher value to families today than the potential construction in the future. Although the credit system has merit and is consistent with general, development, and sustainable communities plans that promote affordable housing on O'ahu, the practice warrants further attention and formalization.

Application of excess credits may conflict with general plan advocacy of diverse communities

One of the general plan's housing objectives is to encourage the fair distribution of low- and moderate-income housing throughout the island. We find that the application of excess credits may conflict with the general plan provision related to diverse communities. Under the credit system, construction of affordable housing can be concentrated in certain development areas, where excess credits can be earned. Those credits can then be applied in another project site, which will reduce the number of actual affordable housing units built. For example, if a developer submits a plan to satisfy an affordable housing requirement using a combination of 50 percent excess affordable housing credits and the balance with an in-lieu fee, it is possible that there will eventually be no construction of actual affordable housing units.

Conclusion

The Department of Planning and Permitting's Planning Division falls short in properly administering its affordable housing responsibilities related to unilateral agreements. While the citywide reorganization in 1998 established responsibilities for the planning division, it had many years to make resource and staffing adjustments to effectively meet its

responsibilities. As a result, poor monitoring, record-keeping, and lack of staff have adversely impacted the department's ability to properly administer unilateral agreements for affordable housing. Additionally, due to the city's inattention to the Housing Development Special Fund, in-lieu fees deposited therein, have not been spent on affordable housing-related initiatives. Instead, we found questionable uses of fund monies. The planning and permitting department's informal use of excess housing credits has a significant potential impact on housing policy and the number of affordable units actually constructed, yet lacks any accountability due to its discretionary application.

We found that the planning and permitting department has not established an effective monitoring program for unilateral agreements with affordable housing requirements. Monitoring activities are inconsistent and reactionary in nature and department staff do not proactively verify developer compliance with unilateral agreement requirements. We also found that the department put minimum administrative effort toward setting up an effective monitoring system in the seven years since the citywide reorganization, and does not maintain an accurate, verified inventory of affordable housing constructed under unilateral agreements. Poor record-keeping practices and reliance on data that was last updated in 2000 hamper the department's ability to assess developer compliance. As a result, the department reports unverified and flawed data to the council and public. The department's inability to inventory and maintain historical data on the estimated 13,000 affordable housing units constructed under unilateral agreements leaves little assurance that the city can substantiate or analyze the effectiveness of the affordable housing program. The department cites lack of staff for its poor monitoring and record-keeping practices.

The city authorizes developers to pay a cash fee in lieu of constructing an actual affordable housing unit. Those fees, which are deposited into the Housing Development Special Fund, are supposed to be collected and spent on alternative affordable housing initiatives. We found that since 1998, no in-lieu fees have been expended for affordable housing-related purposes. Furthermore, there are no plans, goals, or objectives for spending the fees. In-lieu fees collected and deposited in the Housing Assistance Fund, which preceded the housing development special fund, were lapsed into the general fund in 1998. We also found that the housing development special fund is not specifically intended for the development of affordable housing. Since no specific city agency is tasked to monitor, plan, or expend in-lieu fees, the city cannot be assured that in-lieu fees will be used for affordable housing purposes.

We found evidence that in-lieu fees may have been expended for purposes other than affordable housing.

The current framework for the collection of in-lieu fees does not provide a tie-in or feasible basis for significant development of affordable housing. The current fund balance cannot develop a significant amount of affordable housing for sale or rent. Even if adequate monies were available for affordable housing initiatives, communities affected by zoning changes are unlikely to benefit directly from in-lieu fee collections. By amending its in-lieu fee formula, Hawai'i county was able to realize the construction of actual affordable housing units, when virtually none were built prior to the formula's amendment.

The city's general, development, and sustainable communities plans all have an affordable housing component that expresses a desire for the availability of affordable housing throughout O'ahu. We found that the acceptance of in-lieu fees may be inconsistent with, and contrary to, current general, development, and sustainable communities plans related to affordable housing. Limitations on the use of in-lieu fees do not support the city's plans and the city's lack of in-lieu fee expenditures on affordable housing initiatives run contrary to the various plans' desire for affordable housing.

Current rules on unilateral agreements in affordable housing provide developers with reasonable flexibility and options in fulfilling their affordable housing obligations. However, the department of planning and permitting also authorizes developers to bank and redeem excess credits to fulfill housing obligations, without formalizing this practice in rule or ordinance. Although it authorizes developers to bank affordable housing credits, the department does not track or maintain an inventory of excess affordable housing credits maintained by developers, the sale of credits between developers, or the redemption of such credits. Both Hawai'i and Maui county have codified the use of excess credits.

We also found that the department of planning and permitting authorized developers to accumulate excess affordable housing credits contrary to city ordinance during a moratorium on affordable housing conditions. Although Ordinance 99-51 was intended to assist developers in selling their affordable housing units during a downturn in the real estate market, the department authorized developers to bank affordable housing credits in excess of minimum requirements. As a result, some developers were able to bank hundreds of credits for future use. Redemption of the

excess affordable housing credits earned during the moratorium may conflict with the intent of the city's affordable housing program.

In addition, we found that the department's excess affordable housing credit practices are generally consistent with general, development, and sustainable community plans related to affordable housing, but may conflict with the general plan's housing objective advocating a diversity of housing for all income levels in O'ahu's communities. The incentives provided by the use of excess affordable housing credits are consistent with the various plans' tenets that encourage the construction of affordable housing. However, the application of excess credits may conflict with the general plan's advocacy of diverse communities.

Through this audit, we identified several shortcomings with the department of planning and permitting's administration of unilateral agreements in affordable housing and related issues with the management of in-lieu fees and excess affordable housing credits. These are important issues that need to be addressed. However, we also find that the city administration's lack of a dedicated housing entity to guide and manage the city's affordable housing program also contributes to the inefficiencies identified in this report. Under the current system, various city agencies are performing housing *functions* without any guidance, or measurable goals and objectives. In the absence of a housing entity to provide leadership and establish a comprehensive affordable housing program, we believe much of the city's affordable housing efforts will continue to be fragmented and unaccountable.

Recommendations

The Department of Planning and Permitting should:

- a. establish formal policies and procedures for administering unilateral agreements, including monitoring requirements;
- b. maintain a matrix or database with timely data specifying a developer's affordable housing requirement, number of units completed, and outstanding units to be delivered. These figures should be verified by department staff;
- c. initiate systematic record-keeping efforts to account for all affordable housing units constructed under unilateral agreements, as well as track all unilateral agreement ordinances, developers' annual reports,

affordable housing credits, in-lieu fees, site visits, and other pertinent information;

- d. amend the rules for unilateral agreements in affordable housing by establishing an in-lieu fee formula that is consistent with the goals and objectives to be established for the use of in-lieu fees;
- e. amend the rules for unilateral agreements in affordable housing by proposing a framework for the accrual and application of excess affordable housing credits;
- f. track affordable housing credits more closely if it plans to allow continued application of excess credits from one unilateral agreement to another;
- g. establish a procedure where it will document, as part of its housing agreement authorization, how the delivery options exercised by developers conform to general, development, or sustainable community plan provisions related to affordable housing;
- h. report verified affordable housing data in its annual report to the council as required by city ordinance;
- i. evaluate its staffing allocation for unilateral agreement monitoring and, if necessary, redistribute current staff or request the necessary number of positions needed to administer unilateral agreements; and
- j. enforce future ordinance provisions related to unilateral agreements in affordable housing.

The Honolulu City Council should:

- a. consider clarifying Section 6-46.2, ROH, relating to the purpose of the Housing Development Special Fund by specifying whether in lieu fees are intended for *affordable* housing purposes should be an option or requirement;
- b. consider amending Section 6-46.2, ROH, to clarify the use of in-lieu fees for *affordable* housing and allow alternative uses for in-lieu fees collected from developers;
- c. consider amending Section 6-46.3, ROH, to designate a city agency to monitor, plan, and expend in-lieu fees collected by the city; and

- d. consider further review of the Housing Development Special Fund's expenditures.

Response of Affected Agency

Comments on Agency Response

We transmitted a draft of this report to the Department of Planning and Permitting and Department of Budget and Fiscal Services on September 14, 2007. Copies of the transmittal letters are included as Attachment 1. At our exit conference with both departments, we advised the planning and permitting director and the budget and fiscal services director that they would have ten workdays to prepare their written responses to the draft report. The planning and permitting department submitted its response on September 28, 2007, which is included as Attachment 2. The budget and fiscal services department did not submit a separate response; rather, the department deferred to the planning and permitting department's submission.

In its response, the planning and permitting department expressed concern that confidential copies of the draft report were provided to others outside of the department and the mayor's office. The department also questioned the audit's divergence from the initial intent of Resolution 05-285, CD1, which requested this audit. Additionally, the department claimed that there were numerous errors in the draft report and challenged some of our findings and conclusions. Although the department acknowledged that audit staff worked conscientiously to produce the draft report, it commented that many of the errors could have been avoided with simple checks with department staff. The department also suggested that audit staff spent insufficient time understanding their program. However, the department concurred with the following problems revealed in our audit report: that staffing shortages and competing priorities have resulted in the department using subdivision application or building permit review for unilateral agreement compliance instead of monitoring annual reports; that the state of documentation, archiving, and retrieval of documentation is a challenge; that the backlog in reviews and certifications of developer's submittals for affordable housing credits have been reduced; and that the departmental rules used for administering the affordable housing agreements need to be updated.

In reviewing the department's lengthy response, we note that some of the comments, presented as errors or inaccuracies, were clarifying information that enhances the report, but does not have a substantive effect on the audit findings and recommendations. In other instances, the

department commented on issues outside the scope of this audit. We also note that some of the purported errors and inaccuracies were based on information provided to us by department staff or the result of information that the department failed to disclose to us during fieldwork. In those instances, the additional information did not have a material effect on our audit findings. However, we acknowledge the validity of some of the department's comments and have amended the final report to ensure accuracy and clarity.

The department offered several comments on substantive issues that merit comment. The department notes that the report's citation of a one-year residency requirement for receiving credit for an affordable housing unit is incorrect, and that under current rules, the residency requirement is significantly longer and depends on the target income group. The one-year occupancy requirement was confirmed by department staff on two occasions. Furthermore, our review of the *Adoption of Rules for the Terms of Unilateral Agreements Requiring Affordable Housing, 1994*, if these are the rules referred to by the department in its response, do not specify residency requirements based on income group.

The department challenged our finding that in-lieu fees were not expended for affordable housing purposes and clarified that \$3,276,200 was spent on maintaining existing affordable housing in order to preserve the affordable housing inventory, rather than lapsed into the general fund. While this may be the department's understanding of how the funds were spent, the claims are not supported by the files we reviewed at the Department of Budget and Fiscal Services, nor are they supported by a former administration memorandum detailing in-lieu fee lapses from the Housing Assistance Fund or lack of expenditure by the Housing Development Special Fund. We note that the budget and fiscal services department did not submit a separate response to the draft audit report, but deferred to the planning and permitting department's response.

The department also refuted our finding that the planning and permitting department lacks a formal unilateral agreement monitoring process. We clarified in our report that our finding applies to monitoring affordable housing conditions in unilateral agreements only. Nevertheless, we emphasize that our finding is that the department does not have "formal, written policies or procedures" for unilateral agreement monitoring. We commend the department for providing a comprehensive, detailed process for monitoring unilateral agreement requirements. However, this process was not provided in writing to us during fieldwork.

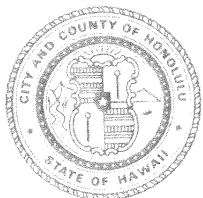
The department challenged our finding that “staff rely on a database that was last updated in 2000.” In its response, the department claims to maintain a database showing affordable housing units credited by projects which is nearly up to date from a three-year backlog. However, this database was not shared with us during our fieldwork. The staff person assigned to certify affordable unit claims submitted by developers confirmed the use of the outdated spreadsheet and made no reference to a database or other source of updated information.

The department disputes our finding that it does not maintain an inventory of the estimated 13,000 affordable housing units constructed under unilateral agreements, or provide a basis for this figure. In its response, the department points to figures in Exhibits 2.1 and 2.2 for confirmation that 13,582 affordable units had been built as of June 30, 2005. As we note in our audit report, the figures reported in Exhibits 2.1 and 2.2 are provided by the developer and are not necessarily what the department has confirmed. In referencing “inventory” we mean actual addresses or tax map key numbers that correlated to the affordable housing unit built. This information is provided to the city and should have been recorded as part of the city’s affordable housing program requirements. By doing so, the incumbent agency can conduct analysis on the affordable units and provide that analysis as a means for developing and amending the city’s affordable housing program over time. We recognize that the apparent lack of a detailed affordable housing inventory preceded the planning and permitting department. However, unless the department commits to constructing an affordable housing inventory for future analysis, the city will continue to operate an affordable housing program without any basis for evaluating program effectiveness or verifying the affordable housing units it actually helped to create.

The department commented that text in our draft report relating to a discrepancy involving returned checks totaling \$118,498 and \$118,552 was confusing and that a quick check in POSSE would have provided an explanation. The department commented further that it is unaware that our office asked the department to explain the discrepancy. We disagree. We requested follow up information on this matter, and others, in a detailed email dated June 2, 2007. Department staff acknowledged receipt of this request for follow up information and advised us on two occasions that staff was working on a response. We never received a response from the department. We further note that had the department responded to our request for follow-up information and clarification, other purported errors and inaccuracies in our draft report could have been addressed.

Additionally, the department characterizes our finding that the department does not document or require developers to justify how delivery options are consistent with general, development, or sustainable communities plan as misguided and incorrect. We acknowledge that the zone change process involves developers explaining how their plans comply with the various regional plans. We submit, however, that the “up front” process may not require the developer to disclose exactly how the affordable housing requirement will be met. The mix of affordable housing units, including the use of in-lieu fees, excess credits, or other delivery options is approved by the department after the zone change ordinance is adopted by the council. Our finding question’s the department’s consideration of regional plan objectives related to the various delivery options approved, if the unilateral agreement is silent on the delivery options used.

Finally, we made other non-substantive amendments for purposes of clarity and style.



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LESLIE I. TANAKA, CPA
CITY AUDITOR

September 14, 2007

COPY

Mr. Henry Eng, Director
Department of Planning and Permitting
650 South King Street, Seventh Floor
Honolulu, Hawai'i 96813

Dear Mr. Eng:

Enclosed for your review are two copies (numbers 12 and 13) of our confidential draft audit report, *Audit of the City's Management of Unilateral Agreements in Affordable Housing*. If you choose to submit a written response to our draft report, your comments will generally be included in the final report. However, we ask that you submit your response to us no later than 12:00 noon on Friday, September 28, 2007.

For your information, the mayor, managing director, each councilmember, and the Department of Budget and Fiscal Services have also been provided copies of this **confidential** draft report.

Finally, since this report is still in draft form and changes may be made to it, access to this draft report should be restricted to those assisting you in preparing your response. Public release of the final report will be made by my office after the report is published in its final form.

Sincerely,

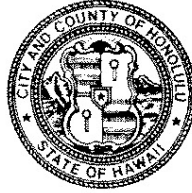
Leslie I. Tanaka, CPA
City Auditor

Enclosures

DEPARTMENT OF PLANNING AND PERMITTING
CITY AND COUNTY OF HONOLULU

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MUFI HANNEMANN
MAYOR



HENRY ENG, FAICP
DIRECTOR

DAVID K. TANŌUE
DEPUTY DIRECTOR



September 27, 2007

'07 SEP 28 P3 53

Mr. Leslie I. Tanaka, CPA
City Auditor
1000 Uluohia Street, Suite 120
Kapolei, Hawaii 96707

C & C OF HONOLULU
CITY AUDITOR

Dear Mr. Tanaka:

Subject: Draft Audit of the City's Management of
Unilateral Agreements in Affordable Housing

Thank you very much for the opportunity to submit a response to the draft audit. We are pleased with the interest taken by the City Auditor's office to learn about the City's affordable housing program, however, we are extremely troubled by the fact that copies of the confidential draft were provided to others outside of the department and the Mayor's office. As evidenced by recent articles in both daily newspapers, information contained in the confidential draft was disclosed to the media. We suggest that the practice of distributing confidential draft copies to those not associated with the agency being audited, be reevaluated.

Upon review of the confidential draft, we find it interesting that at its outset the report summarizes Resolution 05-285 CD1, which requested the audit of the City's affordable housing program, yet chooses to primarily focus on the department's administration of unilateral agreements as it relates to in-lieu fees and credits. Despite its criticism of the in-lieu fee option for developers, the audit fails to acknowledge that no in-lieu fees have been approved by the department in recent years, and that most affordable housing requirements are being met through construction of affordable for-sale units.

The audit comments virtually nothing on the buyback and shared appreciation program, makes only passing reference to the general plan and regional development plans, and says nothing about the appropriateness of the selling prices of affordable housing units developed under this program. Nor does the audit reach a definitive conclusion that the City's affordable housing program has failed to meet its basic objectives.

The principal finding the report makes is that the department's record-keeping could be improved. We agree that there is always room for improvements. But what is

significant is the audit's failure to establish that the department's purported "poor monitoring, record keeping, and lack of staff" has in fact resulted in any appreciable loss of affordable housing opportunities. The program has produced over 13,000 affordable units since its inception. Despite the challenges faced by the department in administering unilateral agreements, we are pleased that the audit's inability to identify any specific incidence of a significant lost opportunity illustrates that at the end of the day, the affordable housing requirements in unilateral agreements continue to be met as projects continue to proceed towards full build-out.

While we know that you and your staff have worked conscientiously to produce this draft, we must note that there are numerous errors which could have been avoided by simple checks with our staff. In addition, as your staff may realize now, the administration of the program is at once, both tedious and complex, and perhaps insufficient time was spent understanding our program, which led to errors in facts and conclusions.

A few examples include:

- The statement on p. 5 that the residency requirement for receiving credit for an affordable unit is for owner occupancy of a minimum of one year is incorrect. That is the requirement that was in place during the moratorium. Under our current rules, the residency requirement is significantly longer and depends on which target income group is involved (eight years for low income households, four years for low-moderate income households, and two years for households earning more than the low-moderate income maximum). Under our proposed rules, the requirement is ten years for all income groups.
- The statement on p. 22 that "electronic documents filed in the department's POSSE system are difficult to retrieve because the file names are not descriptive is incorrect. Documents filed in the POSSE system do have descriptive names, and can be sorted and searched by Description, Author, Last Update, Type, Subject, and Document Number.
- The statement on p. 26 that "the department does not maintain an inventory of [13,000 for-sale and for-rent affordable housing units produced since the 1970s under unilateral agreements] and cannot provide the basis for this figure" is without any merit. Exhibits 2-1 and 2-2 on the preceding two pages reveal a listing taken from the Department's FY2005 Annual Report on the Status of Land Use on Oahu, showing 26 projects with a reported total of 13,582 affordable housing units built as of June 30, 2005.

We have enclosed an errata sheet identifying other errors in the draft audit and commentary for your consideration. It is not exhaustive in terms of addressing the factual flaws and faults but is indicative of the pervasive nature of inaccurate conclusions based on inappropriate or untrained reading of file data.

In spite of factual flaws, we do agree that there are some fundamental problems revealed in your report which require attention.

- Staffing shortages and competing priorities have resulted in the Department using subdivision application or building permit review for UA compliance instead of monitoring annual reports.
- We would concur that the state of documentation, archiving and retrieval of documentation is a challenge that we continue to address. The transfer of files and records from the Department of Housing and Community Development to the Department of Land Utilization and finally to the Department of Planning and Permitting have resulted in information that require considerable effort to retrieve.
- At the start of the audit, the Department had a three year backlog in reviews and certifications of developer's submittals of units for certification for affordable housing credits. We are delighted to report that the backlog has been reduced to six (6) submittals as of today.
- We agree that the Departmental rules used for administering the affordable housing agreements established by Unilateral Agreements need to be updated. We are circulating draft revised rules for comment and will begin the formal procedures (public hearing, etc.) in the very near future.

Finally, we recognize the need for a coordinated approach by the City to address the many aspects of affordable housing. Accordingly, as recommended by the Mayor's Affordable Housing Advisory Committee, the City has a new housing coordinator. She will be pleased to continue discussions with the city council and others on how best the City can use its limited resources to its highest advantage.

Very truly yours,


for Henry Eng, FAICP, Director
Department of Planning and Permitting

HE:ms
Attachment

APPROVED:


Wayne M. Hashiro, P.E.
Managing Director

cc: The Honorable Mufi Hannemann

Errata Sheet

Technical Errors and Omission in the Audit. Commentary by DPP.

1. p. 4 The diagram omits key information. It also has **two errors of fact**. Specifically:
 - In the second box, the DPP **review is of the developer's zone change application** and written statement, rather than a "request" by the developer
 - Also in the second box, DPP, in addition to preparing a report on the proposed zone change, also submits recommendations for consideration by the Planning Commission and City Council, including recommendations regarding conditions requiring affordable housing
 - In the third box, City Council reviews the Director's recommendation in addition to the recommendation of the Planning Commission.
 - Also, In the third box, it is extremely rare for the City Council to hold more than one public hearing on a zone change ordinance
 - Also in the third box, it would be much more accurate to say that the Unilateral Agreement is adopted as part of the zone change ordinance after having been filed with the Bureau of Conveyances, and that an affordable housing condition may be included as part of the UA if the zone change involves residential zoning.
 - In the fourth box, **it is not correct to say that the developer "selects" the delivery option** for meeting its affordable housing requirements. What is correct is that the developer can propose meeting the requirement with one of the listed delivery options. However, the Director must approve the options the developer uses to meet the affordable housing requirement.
 - The listing of developer responsibilities in the fourth box is incomplete. In addition to those listed, developers must:
 - i. Submit reports every six months on the status of compliance with their approved affordable housing agreement
 - ii. Submit buyer qualifications for purchase of affordable units for verification by DPP before sale of the unit can be completed
 - iii. Submit requests for DPP certification of credit for affordable housing unit sales or rentals
2. On p. 5, it is **not correct that the residency requirement for receiving credit for an affordable unit is for owner occupancy of a minimum of one year**. That is the requirement that was in place during the moratorium. Under our current rules, the residency requirement is significantly longer and depends on which target income group is involved (eight years for low income households,

four years for low-moderate income households, and two years for households earning more than the low-moderate income maximum). Under our proposed rules, the requirement is ten years for all income groups.

3. On p. 6, the statement of the department's policy regarding the use of excess credits is **incorrectly stated** with regard to one element of the policy and leaves out another significant element. Specifically:
 - o The recipient project site must be either within the same geographical area or within 7.5 miles of the donor site, rather than "the same development district" as stated in the draft, and
 - o The policy includes the requirement that no more than 50% of the receiving site's affordable housing requirement can be met through use of excess credits, a requirement that is missing from the draft.

Also omitted is the fact that the Director may choose not to approve use of any excess credits.

4. On p. 7, under the heading **Affordable housing credits are based on a sliding scale**, the impression is given by the third sentence that the developer has a free hand in selecting whatever combination of unit types he wants to meet his affordable housing requirement. In fact, the Director has to give approval for the specific mix of unit sizes used to meet the affordable housing requirement, and can insist, for example, that the affordable housing units have the same mix of unit sizes as the market units.
5. On p. 7, under the heading **Developer's implementation plan requires approval**, the second bullet states that the implementation plan must include "supporting information which justifies the type of bedroom mix (**e.g. family size**)". This is not an appropriate example of the information that might be requested. The rules do not include family size as an example of the supporting information that must be supplied, and it is difficult to see how the developer in advance of a marketing campaign would have any idea of the family size of the target group households that might buy or rent the affordable unit. Much more significant from DPP's viewpoint would be how the bedroom size mixture being proposed for the market units compares with that being proposed for the affordable units.
6. On p. 11, under the heading **The City's Unilateral Agreements for Affordable Housing are Managed by the Departments of Planning and Permitting and Budget and Fiscal Services**, the last sentence regarding the Department of Budget and Fiscal Services responsibilities omits the responsibility of BFS to administer the buy-back, transfer restrictions and shared appreciation requirements established by affordable housing conditions in UAs and by requirements of affordable housing agreements between developers and the City.
7. On p. 12, Exhibit 1.4 **incorrectly shows State Special Use Permits as a responsibility of the Development Plans and Zone Change Branch (DPZCB). Special Use Permits**, previously a DPZCB responsibility, are now a

primary responsibility of the Community Action Plans Branch. (A reference to SUPs' at the bottom of p. 13 should also be corrected.) The responsibility for Zoning District Boundary Adjustments which is a primary responsibility of the DPZCB is not shown.

8. On p. 12 and 13, the paragraph beginning at the bottom of p. 12 omits the key responsibility for the Planning Division to prepare long range projections by plan area, sub-area, and traffic analysis zone of future population, housing, jobs, and visitor units for use by infrastructure agencies (like the Oahu Metropolitan Planning Organization) in preparing long range infrastructure plans and to provide basic historic information for analysis of socio-economic and land use trends, and its responsibility for processing amendments to the Public Infrastructure Maps used by the City Council as part of the Capital Improvements Program budget process.
9. The statement on p. 13 in the second sentence that "Prior to FY2004-05, these functions were performed by the Planning and Zoning Program" is **incorrect**. **These functions have been performed by the Planning Division since it was formed in 1999.**
10. The statement at the top of p. 14, that the predecessor agency for the department of planning and permitting in monitoring UAs was the department of housing and community development is **incorrect**. **The predecessor agency with responsibility for monitoring and enforcing compliance with Unilateral Agreements was the Department of Land Utilization (DLU).** In 1999, DLU was merged with the Department of Planning and elements of the Department of Transportation Services, Public Works, and the Building Department to create the Department of Planning and Permitting. Responsibility for enforcing the affordable housing agreements established as a result of affordable housing conditions in Unilateral Agreements was transferred to DLU from the Department of Housing and Community Development when it was abolished by charter in 1998.
11. On p. 14, the first sentence under the heading **City-wide reorganization in 1998 assigned monitoring duties to the planning and permitting department** that "Prior to 1998, the Department of Housing and Community Development administered unilateral agreements" is **incorrect**. A correct statement would be that **"Prior to 1998, the Department of Housing and Community Development administered affordable housing agreements required as a condition of Unilateral Agreements adopted by the City Council as part of zone change ordinances."** As noted above, prior to 1998, the DLU administered the unilateral agreements adopted as conditions of zone changes, with the Monitoring and Compliance Branch of DLU having the primary responsibility for the task. When the DLU was merged into the DPP in 1999, it brought the UA monitoring responsibilities with it, including the responsibility for monitoring affordable housing agreements which it had received with the abolition of the DHCD in 1998. At that time, the responsibility for UA monitoring, including monitoring of affordable housing agreements, was moved from the

Monitoring and Compliance Branch to the Development Plans and Zone Change Branch.

12. The discussion on p. 14 about events following the city-wide reorganization fails to include other relevant information regarding the background for the Planning Division's assumption of the responsibilities for monitoring and enforcing compliance with affordable housing agreements required as a condition of Unilateral Agreements, including:
- The adoption in 1999 of what turned out to be a five year moratorium (under Ord. 99-51 and Ord. 01-33) of key aspects of the affordable housing agreements, including requirements for buyer qualification, owner occupancy, buy-back requirements, transfer restrictions, and buy-back and shared appreciation requirements; and
 - The requirement to provide two major studies (in 2001 and 2005) of the impacts of the moratorium on delivery of affordable units to target groups.
13. Page 18, Item 2. Contrary to the statement that in-lieu funds have not been expended for affordable housing related purposes, funds were spent on maintaining existing affordable housing in order to preserve the affordable housing inventory.
14. The statement on p. 18 that the department of planning and permitting "lacks a formal unilateral agreement monitoring program" is **incorrect** and reflects a **continuing confusion throughout the draft** between the monitoring and enforcement of affordable housing agreements required as a condition of Unilateral Agreements and the larger program which is the monitoring and enforcement of all the conditions of Unilateral Agreements.

The reference on p. 19 to 1983 Department of Housing and Community Development (DHCD) guidelines and the implication that there is a problem that the "current planning division administrator was unfamiliar with these guidelines and did not have a copy" is particularly mystifying.

In 1983, the responsibility for monitoring and enforcing compliance with UA conditions was with the DLU, not DHCD, and the rules and procedures for dealing with UA conditions were brought into the DPP by the DLU staff when they became part of the DPP.

As a result, **the DPP does have a formal UA monitoring and enforcement program, which is the descendant of the DLU program**, and includes:

- Provisions in the Land Use Ordinance establishing conditional zoning,
- A well established process by which the Department analyzes proposed zone changes, considers public review comments, and prepares recommendations to the Planning Commission and the City Council for appropriate conditions, including affordable housing conditions, needed to mitigate adverse project impacts and to implement General Plan and Development Plan and Sustainable Communities Plan policies;

- A well established process by which advisories are issued as zone change ordinances are adopted, alerting processing staff to send subdivision and building permit applications for projects with adopted UA conditions to the Development Plans and Zone Change Branch for reviews to certify compliance with those conditions;
 - Permit processing subprograms in the POSSE system which request and collect the UA compliance reviews for building permits and subdivision applications;
 - A record of using those permit reviews to determine if compliance with UA conditions, including compliance with affordable housing UA conditions and terms of affordable housing agreements, can be documented, and when documentation is not available, refusing to issue subdivision approvals or building permits until the required documentation is provided by the developer;
 - A trail of electronic and hard copy documentation of these compliance reviews, and the resulting customer submittals demonstrating compliance; and
 - Requirements in the LUO and stated as a condition in many UAs that developers provide an annual report of compliance with UA conditions.
15. The statement on p. 19 under the heading **Unilateral Agreement administration is inconsistent and reactionary in nature** that DPP “monitors unilateral agreements in two primary ways”: completion of a monitoring report annually and review of developer annual reports is **not correct**. Our staff monitoring reports are working documents that are reviewed and updated as new information on UA compliance is collected, whether as part of a permit compliance review or the arrival of a submittal by a developer. **For active projects, the staff monitoring report will be reviewed and updated multiple times throughout the year, not just annually**. That is because the DPP staff reviews UA compliance in the most fundamental way possible: **Whenever there is a permit or subdivision application for a project with UA conditions, we ask if there is documentation of compliance with the specific conditions established in the UA.**
- The compliance check starts with **a review of the conditions of the UA** to see exactly what is required by the wording adopted by Council.
 - Next there is **a review of all available sources** to see what documentation they provide of compliance. Among the sources reviewed are:
 - i. the **latest monitoring report** to see what annotations were made during previous compliance reviews,
 - ii. the **POSSE electronic files** to see what scanned reports and submittals are on file there, including the most recent annual report, and

- If after completion of these reviews, we are unable to find documentation of compliance, we will indicate in our review that the permit or subdivision application cannot be approved until we receive the appropriate documentation.
 - We find that the required documentation, including any annual or semi-annual reports that the developer may have failed to submit, shows up rather quickly when developers find they cannot get their subdivision or building permit approved.
 - All documentation submitted is scanned and then sent to DPP's Data Access and Imaging Branch (DAIB) to be filed, and the staff monitoring report is annotated to recognize the receipt of the compliance documentation.
16. The statement on p. 19 in the last paragraph that "developers do not routinely submit annual reports" is **incorrect**. **Most major developers, including Castle & Cooke, Gentry, DR Horton/Schuler, Campbell Estate, and Haseko, do submit annual reports as required.** It is true that developers sometimes fail to submit annual reports if their projects are not active or if the project has been completed.
17. We ask that a listing be provided of the 18 "unilateral agreement files" missing all required annual reports which is reported in the last sentence on p. 19. We note that, **technically, we do not maintain any "unilateral agreement files."** All documents related to specific unilateral agreements are filed in the file for the zone change under which the UA was adopted. In addition, in recent years, as we have received or retrieved documents pertinent to specific UAs, we have scanned the documents, to the extent practical, and filed them electronically in the POSSE system as part of the document collection associated with the appropriate zone change job. **The report should be clarified to indicate if the 18 files reviewed were the official zone change files maintained by DAIB and/or printouts of the electronic zone change files contained in the POSSE system.** The report should also be clarified to indicate if the projects involved are active projects, how many had UAs with a specific requirement for submittal of an annual report, and if there were annual reports for either the most recent year or the preceding year.
18. The statement on p. 20 in the last paragraph that "Prior to the planning division's administration of unilateral agreements, the former housing and community development department's Monitoring and Compliance Branch monitored zone change conditions, including unilateral agreements" is **incorrect**. It was the **DLU's** Monitoring and Compliance Branch that had responsibility for monitoring and enforcement of Unilateral Agreement conditions.
19. The statement on p. 21 in the heading **Staff rely on a database that was last updated in 2000** is incorrect. **We do not use (or rely on) the spreadsheet that is referred to in the following paragraph. We maintain a database showing affordable housing units credited by projects which is nearly up to date (from a 3 year backlog). We also maintain project specific files which**

include reports on compliance with affordable housing conditions and other UA conditions and are updated as soon as new documentation and research results are obtained. The spreadsheet in question was inherited from the DHCD by the Monitoring and Compliance Branch who apparently did use it to track affordable housing compliance from 1998 to 1999.

20. The statement on p. 21 in the fourth sentence under the heading **Staff rely on a database that was last updated in 2000** that “The planning division staff responsible for monitoring unilateral agreements estimates that it would take two staff persons 400 work hours to research and update the 2000 list” is **incorrect. Neither of the two persons directly responsible for monitoring unilateral agreements, Mr. Eugene Takahashi and Mr. Bob Stanfield, made such a statement to the Auditor.**

The late Mr. Dave Matsushima who came to the Planning Division from the Monitoring and Compliance Branch may have made these comments. His sole responsibility at the time of the audit was to do certifications of affordable unit claims submitted by developers.

21. The statements in the second paragraph on p. 21 under the heading **Staff rely on a database that was last updated in 2000** omit key information needed to understand the context of the answer provided to the question stated as “At any given time, can you identify 1) a developer’s affordable housing requirement, 2) how many affordable housing units the developer has constructed, and 3) the outstanding number of housing units/credits?” Staff indicated that the answer was not immediately available and required consultation of hard copy files and Posse.

Determining the developer’s affordable housing requirement is easily obtained by opening the POSSE system and using its electronic document retrieval functions. It is more challenging, however, to determine how many credits the developer has earned and how many more are required.

As developer’s request confirmation of compliance, or projects approach buildout, or as needed to meet Administration or Council requests, we have done the investigative work needed to document and determine definitive answers to these questions. Reviews have been completed in the last few years for Makakilo, Royal Kunia Phase I, Ewa by Gentry, Ko Olina, and the Villages of Kapolei.

22. The statement in the first sentence of the first paragraph on p. 22 that “there are no standard procedures for information intake” is **incorrect. There are well established standard procedures for information intake at DPP.** All information submitted to the Department of Planning and Permitting is time-stamped and assigned to the responsible Division for processing as appropriate.

Documents relevant to affordable housing conditions established by Unilateral Agreements are routed to the Planning Division where they are logged into the POSSE system, scanned, and sorted, depending on whether some response or action is required or whether they should be just reviewed and filed.

Annual or semi-annual reports by developers are scanned into the relevant POSSE zone change job, and the hard copy is sent to DAIB for filing in the official zone change file.

Requests for affordable unit certifications are scanned, a correspondence job (ELOG) is created in POSSE, and the job is assigned to staff who are responsible for updating the database on affordable housing unit submittals and certifications, gathering the information needed to review eligibility, and preparing a response to the developer, indicating how many credits have been awarded and explaining any requests that have been denied. A copy of the signed response is scanned into POSSE and a hard copy sent to DAIB for filing.

Developer proposals for new or amended affordable housing are scanned, a correspondence job (ELOG) is created in POSSE, and the job is assigned to staff who are responsible for reviewing the agreement for compliance with applicable rules, preparing recommendations for revisions, submitting agreements to the Corporation Counsel for review for form and legality, and preparing responses to the developers, indicating any needed revisions or transmitting the approved agreements when an agreement has been approved and signed by all parties. A copy of all signed responses and transmittals associated with the agreement review is scanned into POSSE and a hard copy sent to DAIB for filing.

23. The statement on p. 22 in the third sentence under the heading **Poor record-keeping practices hamper the department's ability to assess developer compliance** that "electronic documents filed in the department's POSSE system are difficult to retrieve because the file names are not descriptive" is **incorrect**. **Documents filed in the POSSE system do have descriptive names**, and can be sorted and searched by Description, Author, Last Update, Type, Subject, and Doc. No.
24. The statement on p. 22 in the fourth sentence under the heading **Poor record-keeping practices hamper the department's ability to assess developer compliance** that "The monitoring report for the Mililani Mauka project, Ordinance 95-56 . . . has a file name 89/Z-006." is **incorrect**. **There is no staff monitoring report for Ord. 95-56 because it has no Unilateral Agreement conditions**. Ord. 95-56 (Posse Job No. 94/Z-1) discontinues application of one UA and indicates the conditions of another UA will continue.

DPP Job No. 89/Z-6 refers to the zone change job that resulted in adoption of Ord. 89-123. Ord. 89-123 does have a UA and does have a staff monitoring report, last updated on April 26, 2006.

The reported difficulty of the administrator trying to find the monitoring report in POSSE is understandable since the staff monitoring reports are not filed in POSSE. As continually updated staff working files, they are maintained on the Department's document server. The file name and path under which the staff monitoring report is filed is printed in the header of the first page of the staff monitoring report. In addition, a cross-index for all zone changes with a UA is maintained on the Department document server which can be used to locate the POSSE files or staff monitoring reports for each ordinance with a UA.

In March 2007, at the opening of the audit, the Auditor was provided a copy of the Division's cross-index to all known zone changes with UAs. That index gives the Ordinance Number, Project Name, Posse File #, Tax Map Key, and Status Report File Name and Path for all zone changes with UAs. The index has no listing for Ord. 95-56 because it is not one of the zone changes with a UA. The index does provide the Status Report File Name and Path for the UA associated with Posse Job 89/Z-6 (Ord. 89-123).

Reports are easily retrievable by branch staff responsible for UA monitoring.

25. Without the specific file numbers, we cannot determine the accuracy of the finding on p. 23 in the first paragraph that "18 development project files with unilateral agreements, which included 26 separate unilateral agreement ordinances ... lacked 12 of 26 ordinances."

However, as noted previously, when the Planning Division assumed the UA monitoring responsibility in 1999, staff obtained and scanned into POSSE all the ordinances for zone change with UAs. It is those scanned documents that we retrieve when we need to have the exact language of the UAs. In addition, our staff monitoring reports, which are maintained on the DPP document server, provide close paraphrases or exact quotes of the specific conditions in the UAs.

26. The statement on p. 23 in the 6th sentence in the paragraph under the heading **The department reports unverified and flawed data to the council and public** omits key information that materially affects the conclusion stated in that heading.

The statement "A department staff person we interviewed acknowledged that the department's annual report data on the status of affordable housing is not accurate" requires clarification. **The annual report data is an accurate statement of what developers report is the status of their affordable housing requirements and credits.** On p. 8 of the FY2005 annual report, the third paragraph clearly states that the "information shown in the three tables [Tables II-1, II-2, and II-3] is the developers' own estimates and tentative timetables." In addition, the footnote for the Table II-1 column reporting affordable units required by UA states that ". . . Both the number of units and the construction schedule are the developer's own plan."

At the onset of the audit, the department was three years behind in certification of affordable housing credits which may have resulted in some discrepancies in the data. The department is now current in certification.

27. The last sentence on p. 23 is **incorrect**; Exhibit 2.2 shows data taken from the department's annual report which was **correct as of June 30, 2005**, not 2006.
28. The second sentence in the paragraph at the bottom of p. 25 **incorrectly reports** what the Director's letter to Mr. Shinobu Takara, Project Manager of Haseko Homes, Inc. says. The letter does not state that "the developer fulfilled its affordable housing requirement of 771 units by constructing 788 units." In fact, the letter reports that the approval of one affordable housing credit requested for the July 6, 2004 period 'will fulfill the affordable housing requirement of 771

affordable units for area 1 and 2. The total approved credits for the project is 821.” There is no reference to 788 units in the letter.

29. The statement in the third sentence in the same paragraph that “the actual number of units reported [in the department’s FY05 Annual Report on the Status of Land Use on Oahu] overstated the [Ocean Pointe] developer’s actual contribution by 33 units” is **incorrect**. The FY05 Annual Report states that 821 affordable units had been built. That is exactly the number of credits that the Director’s October 13, 2004 letter states have been approved for the Ocean Pointe project and is consistent with the approvals summarized in Mr. Takara’s September 13, 2004 submittal.

(We agree that the affordable housing units required for Ocean Pointe should be shown as 771 units, instead of 821, indicating that Ocean Pointe built and sold 50 more affordable units than required. In addition, it would be more correct if future Annual Reports reported affordable credits awarded rather than units built and explained that each credit is the equivalent of a two-bedroom unit.)

30. The statement on p. 26 that “the department does not maintain an inventory of [13,000 for-sale and for-rent affordable housing units produced since the 1970s under unilateral agreements] and cannot provide the basis for this figure” is **incorrect**. Simple examination of Exhibits 2-1 and 2-2 on the preceding two pages in the draft audit would reveal a listing taken from the Department’s FY2005 Annual Report on the Status of Land Use on Oahu, showing 26 projects with a reported total of 13,582 affordable housing units built as of June 30, 2005.
31. The statement in the first sentence in the last paragraph on p. 26 that “A planning division administrator notes that when the former department of housing and community development was eliminated in 1998, the department of planning and permitting assumed the responsibility for monitoring unilateral agreements” is **incorrect**. As explained above, **the Department of Land Utilization had the responsibility for monitoring Unilateral Agreement compliance prior to this Department**. The Department of Housing and Community Development administered housing agreements required by Unilateral Agreements.
32. The statement at the end of the second paragraph on p. 28 that “From FY1992-93 to FY2005-06, the city has collected nearly \$4.5 million in in-lieu fee payments from developers for affordable housing requirements” should be put into context. The lion’s share of those payments were made prior to 1998 when the Department of Land Utilization assumed the responsibilities for the affordable housing program, and the negotiations with developers over how their affordable housing requirements should be met. As shown in Exhibit 2.4, \$3,276,200 of the in-lieu fees were collected under agreements negotiated by the DHCD. In the last few years, the Department has not approved any in-lieu fee payments.
33. Page 31. The \$3,276,200 collected for in-lieu fees were expended by DHCD between 1992 and 1998 for affordable housing programs.
34. The statements in the first paragraph on p. 33 are incorrect and confused. It is a fact that the Department of Planning and Permitting returned checks totaling

\$118,498 to DR Horton/Schuler in June 2004. It is also a fact that the a check for \$118,552 from DR Horton/Schuler was deposited into the Housing Development Special Fund in June 2005 as the Department of Budget and Fiscal Services reported. The explanation is quite straight forward.

In the Department's letter of June 22, 2004 (DPP File No. 2003/ELOG-3247), we explained that, after a lengthy review of the documentation for residential projects and affordable housing credit awards for Finance Realty projects in Makakilo, we are returning two checks for in-lieu fees submitted by DR Horton/Schuler for their Makakilo projects (which they had taken over from Finance Realty). It was our determination that sufficient credits had been awarded for the earlier Finance Realty projects in Makakilo to establish a surplus sufficient to meet the affordable housing requirement for the Makakilo projects that DR Horton/Schuler was developing and so no in-lieu fee was owed.

However, on July 22, 2004 (DPP File No. 2004/ELOG-1732), DR Horton/Schuler responded that Finance Realty had refused to release the surplus credits for DR Horton/Schuler's Makakilo project and as a result, they wished to resubmit an in-lieu fee payment of \$118,552. It was this payment that was eventually approved and deposited in June 2005.

The reason why two checks were returned in 2004 and a new check was deposited in 2005 was easily determined by reviewing the correspondence on file in the POSSE system. However, we are not aware that the Auditor asked us to explain the "discrepancy."

35. The statements in the third paragraph on p. 39 that the Department of Planning and Permitting "does not report or document general, development plan, or sustainable community (sic) plan compliance in its unilateral agreement options in affordable housing" and that "The department also does not document or require developers to justify how developer delivery options, including in-lieu fees, are consistent with general, development or sustainable community (sic) plans" are **incorrect and misguided**.

These statements ignore the fact that the Unilateral Agreements are adopted as part of zone change ordinances. As part of the processing and adoption of zone change ordinances, the developer has already submitted a written statement that includes an assessment of how the proposed zone change will be consistent with the General Plan and relevant Development Plan or Sustainable Communities Plan; the Department has analyzed the compliance of the zone change with the General Plan, and the relevant Development Plan or Sustainable Communities Plan; and the Council, in adopting the zone change ordinance, is required by Charter to find that approving the ordinance is consistent with the General Plan and the relevant Development Plan or Sustainable Communities Plan.

Accordingly, there is no need to "report or document" compliance with the General Plan or Development Plan when implementing an aspect of the zone change ordinance since the Council, as the ultimate authority on the General Plan and Development Plans, has approved the zone change and the conditions of the associated UA as being in compliance.

In a similar fashion, the Department does not report or document compliance with the General Plan or relevant Development Plan when it applies height limits, requires landscaping improvements or traffic improvement requirements, reviews urban design plans or implements any of the other controls and requirements affecting the property covered by the zone change ordinance.

What is required is to report and document that the conditions of the Unilateral Agreement are being complied with. As we process the subdivision and permit applications submitted by the developers, we continually evaluate where they are with respect to each of the conditions, and document the results of our evaluations, and the specific conditions that must be met before the applications can be approved.

36. The statement at the bottom of p. 42 that “the department [does not] formally track the balance, sale or redemption of these [excess affordable housing] credits” is **incorrect**. We do formally track the balance and the excess credits cannot be redeemed unless the Director approves it as part of an affordable housing agreement.
- We formally track the number of credits that have been requested and awarded to each project and maintain that information on a spreadsheet.
 - On a project by project basis, as is most critical, we do inventories of all the documentation, and make a formal determination of what the final affordable housing requirement is, how many credits have been earned, and how many of those credits are “excess.” For example, such assessments have been completed for Finance Realty’s projects in Makakilo, for Halekua Development’s Royal Kunia Phase I project, and for the Hale Alii project in Hawaii Kai.
37. As noted previously, the one year owner occupancy requirement for for-sales affordable units was true only during the moratorium. The second sentence in the paragraph at the top of p. 43 should be corrected.
38. The statement on p. 43 in the second paragraph that “The department of planning and permitting ... does not maintain any formal, written policies or procedures regarding the accrual, application or transfer of affordable housing credits...” omits to mention that formal rules for the transfer of excess affordable housing credits have been drafted and are scheduled to be sent out for public hearing in the near future, and that the policy that would be established by the draft rules is the policy that the Department has been following informally for the past few years in approving or denying developer proposals.
39. The statements on p. 43 in the last paragraph regarding how use of excess credits would be approved are incorrect. Use of excess credits to meet a developer’s affordable housing requirement has to be established as part of the Director’s approval of either an initial affordable housing agreement or the amendment of an existing affordable housing agreement. There is no requirement that the Director has to approve the use of excess credits if requested by a developer.