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Local Intel: Impact Embargo

Orange County, Calif., postpones fee collection, but what will the effect be on the market?

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Disneyland may be the happiest place on Earth, but production home builders in the market have little to smile about these days. Without the rampant price appreciation and lax lending requirements characteristic of Orange County during the boom years from 2004 to 2006, consumers now faced with diminishing affordability remain on the sidelines, according to Hanley Wood Market Intelligence.

But is it possible that the situation could be about to change for the better?

Thanks largely in part to the efforts of the Building Industry Association of Southern California, Orange County chapter, local elected officials recently agreed to postpone the collection of impact fees for new-home construction until project completion for one year, at which point the issue will be revisited and evaluated in light of economic conditions at that time.

"Typically, development impact fees are paid early on; the ability to delay that until [project completion] lightens the finance cost that goes into the overall house," explains Strategic Land Advisors principal Paul F. Grover. "[If you're] able to defer that financing, that in turn makes the house more affordable."

Postponing the collection of such fees–thereby lightening the builder's financing costs and ultimately lowering the price of the home–stands to reason, according to Grover, because the impacts related to those fees don't really take effect until the buyer closes escrow.

"Water, parks, schools, traffic–those impacts are pretty much occurring only when people have moved in," he says. "Open space, storm drains–those fees are an impact at the construction of the project, so those you could argue should not be deferred. The good news is people are looking at it, and the jurisdictions that are charging the fees are willing to at least discuss it."

The impact fee postponement will undoubtedly put precious dollars back in the pockets of home builders–and the timing couldn't be better.

"I think the effect will be positive in the short run since it is a real cost savings; anything that can be done to ease the cost burden in this environment is helpful," notes Sullivan Group Real Estate Advisors president Tim Sullivan.

Yet the anticipated effect on new-home sales appears minor at best, according to Sullivan. "The issues with home sales in California have much more to do with the consumer's perception that prices are going to drop further (no urgency), their inability to find a mortgage (stringent underwriting), and their lack of confidence in the market and economy as a whole," he says.

And the recent strides taken in Orange County could potentially be extended statewide, as the CBIA is supporting a bill that would require local governments to meet with building advocacy groups in their area in order to reach an agreement on impact fees.

"I think it makes sense," Sullivan says. "New development should shoulder its fair share of infrastructure costs, but expecting fees to continue to increase–or even stay the same–in a declining market is unreasonable."

Few, if any, would argue that the measure would not provide relief to an industry in dire need of such assistance. But whether it's enough to make an appreciable difference remains up for debate.

"Although the postponement of fees to final inspection would help builders, their ability to sell a home will be the prevailing force behind whether they start construction on the next phase," notes Billy T. Chen, principal of Land Co. Development Resources. "Any stimulus that increases affordability and consumer confidence will be 1,000 percent more effective than fee reductions or postponement in payment. In this market, if a builder knows they can sell the home and break even at the end of the day, they will build it."

Sin City Spotlight

Despite a contraction in 1Q2008, the job market in Las Vegas has been strong over the past five years, with healthy increases in transportation and utilities, as well as the government sector, according to Hanley Wood Market Intelligence. And with no personal income tax and annualized population growth of 4.0 percent posted for 1Q2008, industry experts define it as down, but certainly not out.

"The key in that market is burning through the foreclosures and getting pricing back to a reasonable level," says Tim Sullivan of Sullivan Group Real Estate Advisors. "The flipside of decreasing prices is that affordability is increasing. Apartment vacancy is up over the last year as investors have offered their units for rent. This 'shadow market' has stolen renters from the classic apartment market."

Visitor numbers remain strong in Vegas with over 39 million expected in 2008, Sullivan notes. However, gaming revenue was down in the first quarter. "[Still], projected population growth is a plus for potential demand, with approximately 270,000 additional people expected to enter the market in the next five years," he points out.

Sullivan points to MGM Mirage's City-Center development as a bright spot in the market, thanks to its high-end and international clientele, as well as to the Sun City Anthem and Del Webb Solara brands as the market leaders for detached single-family product, based on strong community appeal and the fact that–as with CityCenter–the buyer remains discretionary. "While they are more cautious because of market conditions, if they see what they want, they will pursue it," he says.