Mayor and Members of the City Council

STAFF REPORT

For the Meeting of July 14, 2025

Title/Subject

Resolution 2381 – Development Incentive Agreement with The Hub Hermiston, LLC.

Summary and Background

This resolution will approve a development incentive agreement intended to stimulate the construction of approximately 276 market-rate apartment rental units.

Structure

The basic thrust of the agreement is that the City of Hermiston will pay the developer cash equal to approximately 66% of what they will have paid in property taxes from now through 2031. It is important to understand that this means that it is not a tax exemption. The developer will be required to pay all of their regular property taxes as normal, which means that all of the underlying taxing entities (i.e. Hermiston School District, UCFD1, City, etc.) will receive property tax revenue from the development just the same as if this agreement didn't exist. However, the developer will then provide proof of payment to the City each year, and then the City will pay them certain amounts each year relative to what they actually paid to the County assessor's office.

The agreement will have the City paying the developer an amount equal to 100% of their 2026 & 2027 property tax bills, 75% of their 2028 bill, 50% in 2029 & 2030, and 25% in 2031. The agreement is intended to act as a "carrot & stick" incentive by setting these amounts to specific dates. Since the city will only pay a percentage of the property tax actually paid by the developer, then if the developer wastes a year before building, then they will have squandered a year of their highest incentive rate.

Table 1. % of Total Property Tax Bill Paid For by City of Hermiston By Year					
2026	**2027**	**2028**	**2029**	**2030**	**2031**
100%	100%	75%	50%	50%	25%

Justification

The City Council has had support of housing development as one of it's annual goals every year since 2017, and consistently, whenever we do community outreach or polling, the availability of housing and the cost of housing, always shows up clearly as something that the community prioritizes.

<u>The Case for Market-Rate Rentals</u>

Hermiston has relatively little problem attracting developers to build relatively affordable detached single-family homes for sale. Hermiston has averaged roughly 108 single family homes built per year since 2020.

Hermiston also has relatively little problem attracting developers to build income-restricted rental units. Hermiston has averaged 28 income restricted units per year since 2019.

Hermiston has had exactly zero market-rate apartment units built over the past 10 years. The reason for this is that, although land in Hermiston is relatively more affordable, land is only a small portion of the overall cost of a development; whereas most of the other costs to develop (i.e. lumber, appliances, etc.) are the same whether they build in Hermiston, Portland, Bend, Kennewick, or elsewhere. However, the rents which developers can achieve are much higher in those other markets. Therefore city staff has been told by multiple developers that although they agree that there is a market need for apartments in Hermiston, they can make more profit by charging higher rents in other markets.

To highlight why this dynamic is a problem, I always like to set up a hypothetical example of the 22 year old who just graduated from college and got a job teaching in Hermiston. They show up looking for a place to live, and we, as a community basically say, "well, you can buy this $300,000 house, try to get a subsidized apartment, or rent a house for $1,800 per month."

Now, as a single person household earning the starting teacher salary of $50,000, they don't come close to qualifying as "low-income" for the purposes of subsidized housing, so that's not an option. Then, since they're still in their formative years, without "roots" in the community, they very well may not want to lock in to buying a house right out of the gate; even assuming that they could afford it while paying back whatever student loans they have. So finally, they look at market-rate rentals and realize that they can get the same rents in Tri-Cities and enjoy all the benefits that a larger community affords a young adult. So they end up renting in south Kennewick and commute down every day for work.

Losing that 22 year old to living in Kennewick ends up having a lot of long-term economic impacts for the community if we follow them through a logical life pattern.

Eventually, they will buy a new car from a dealer there, they will get all of their oil changes there and buy their insurance from a local agent there. They will also go out to eat and support all of the restaurants in Tri-Cities using their Hermiston School District salary, to say nothing of all of the other stores that they will support up there with their patronage.

Of course, this person will find a significant other who lives close to them in Tri-Cities and probably works in Tri-Cities. They will eventually get married, and since both spouses now have ties to the Tri-Cities, they will end up buying a home there. This teacher still won't mind commuting down every day for awhile, but eventually, once the babies start coming, that will get more and more challenging until they eventually leave the Hermiston School District and take a job in Tri-Cities. They will have their kids in Tri-Cities schools, take them to doctors/dentists/etc. there, and buy all of the things that kids need there.

All of this adds up to a massive loss of investment and potential spending in Hermiston.

On the other hand, if we have an "on-ramp" in to the community for the young teacher to begin living here, then eventually all of those things will happen in Hermiston. They'll meet another teacher, get married, have kids, buy a house, and suddenly just 10 years after they first moved here, they now represent a stable family making $150,000 per year contributing significantly to the local economy.

This type of situation, when aggregated across dozens of examples per year, really adds up to economic development in the form of jobs to meet the needs of a family, from teachers to nurses, to insurance agents, mechanics, restaurant workers, retail workers, dental hygienists, on and on and on. It all boils down to trying to keep dollars earned locally circulating in the local Hermiston economy, rather than exporting them to Tri-Cities where they're lost forever.

<u>Our Partner: The Hub Hermiston, LLC</u>

The developer has a large portfolio of similar developments across the pacific northwest, including the "Westgate Apartments" which they constructed in Pendleton about 5 or 6 years ago. Staff feels comfortable with the developer's track-record and ability to deliver on their commitment.

<u>The Development</u>

The development is proposed for a 12 acre property generally to the northwest of the Diagonal Blvd. and NE 10th intersection. A preliminary site plan which shows the proposed layout is attached to this staff report. The developer intends to build a sustainable mixture of apartment units with varying numbers of bedrooms to meet market demand.

Tie-In to Council Goals

1.7: Attract market-rate rental housing developments to increase middle housing inventory.

1.8: Study incentive options for market-rate rental housing.

Fiscal Information

The approximate total estimated cost of this incentive package is $1.3 million. While that may sound large on it's face, it is important to remember the scope, and the market. This covers 276 units, which means the incentive works out to a per-unit cost of $4,856. Market-wise, many folks probably remember that Morrow County was offering $5,000 per home incentives dating back to at least 2012; which is equivalent to $7,000 per unit in today's dollars. On the other end of the stratosphere, Gilliam County, in May announced a plan to spend $1.25 million to develop buildable lots for 12 housing units, for an eye-watering taxpayer subsidy of $104,000 per unit.

<u>How the Estimate Was Reached</u>

Total Valuation- Staff looked at actual property taxes paid for comparable properties in Hermiston, and scaled that up by 276 units to arrive at an estimated total annual property tax bill of $564,000 per year.

Tax Roll/Buildout Timing- A major variable at play is how quickly the development builds-out and receives certificates of occupancy; thereby placing it on the tax rolls by January 1st, which results in taxes owed by that following November. Based on construction timelines and market absorption, staff assumed that the full taxable value would not hit the rolls until 2029, following the below anticipated schedule.

Table 2. % of Estimated Value On Tax Rolls Estimated by Year					
2026	**2027**	**2028**	**2029**	**2030**	**2031**
5%	40%	90%	100%	100%	100%

Total Taxes Paid- Using the above assumption, staff projects that the development will pay property taxes to the County Assessor approximately as shown below.

Table 3. Estimated Annual Property Taxes Paid by Year					
2026	**2027**	**2028**	**2029**	**2030**	**2031**
$28,217	$225,738	$507,911	$564,346	$564,346	$564,346

Taxes Received by Taxing Entities- To be clear, all of funds shown in Table 3 will make their way to all of the existing taxing districts as normal. That includes the City of Hermiston, which receives approximately 29% of all local property taxes.

Table 4. Estimated City of Hermiston Tax Revenue Received by Year					
2026	**2027**	**2028**	**2029**	**2030**	**2031**
$8,087	$64,699	$145,573	$161,748	$161,748	$161,748

Estimated Cost Owed to Developer- Combining the amount paid in taxes shown in Table 3, with the incentive schedule shown in Table 1, the estimated amount owed back to the developer is shown below in Table 5.

Table 5. Estimated Amount Owed to Developer by Year					
2026	**2027**	**2028**	**2029**	**2030**	**2031**
$28,217	$225,738	$380,933	$282,173	$282,173	$141,086

Net City General Fund Share- In order to cover the cost owed to the developer in Table 5, it is intended to leverage General Fund tax revenues directly attributable to this development, as shown in Table 4. When subtracting Table 4 from Table 5, we are left with an un-funded margin.

Remaining Margin- The remaining margin which must be covered by other City of Hermiston resources. That margin, planned to be covered in large part by Enterprise Zone resources, is shown in Table 6.

Table 6. Estimated to Be Covered by Other City Resources					
2026	**2027**	**2028**	**2029**	**2030**	**2031**
$20,130	$161,039	$235,360	$120,425	$120,425	($20,662)*

**City Tax Revenues (table 4) are expected to exceed total cost owed to developer (table 5) in 2031.*

<u>Net Costs</u>

Refunded City General Fund Revenue:	$703,603
<u>Other City Resources (Ezone):</u>	<u>$636,717</u>
Total Cost Paid to Developer:	$1,340,320

Liability/Strategy
It is easy to look at 276 housing units, and equate that to 276 more households who will have domestic disputes needing police response, or driving on our streets, using our parks/library/etc., and assert that the City will need that general fund revenue in order to provide those services. However, it is also important to recognize that the City's financial liability scales with that demand for services. The way that this incentive is set up, there is no financial liability if there is no development.

Strategy-wise, this structure is slightly different than a similar program in Pendleton, which got a little more nuanced and gave credit to the developer for units which had yet to be occupied. This structure sets a rigid incentive structure which is agnostic of whether any of the finished units (which they are paying tax on) are actually occupied or not. Therefore, the developer is incentivized not only to build as quickly as possible, but also to fill the units up as quickly as possible. Otherwise, in the Pendleton model, it may be preferable to set an aspirational rent amount and sit on vacant units hoping to set the new market rate. In our model, the developer is incentivized to quickly bring the rents to an affordable market rate in order to fill them as quickly as possible with paying tenants in order to help pay their tax bill.

Alternatives and Recommendation

Alternatives

1. Approve resolution 2381
2. Reject resolution 2381

Recommended Action/Motion

Motion to approve Resolution 2381

Submitted By:

Mark Morgan