
Journal of Case Study Research:

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CENTER FOR
CALIFORNIA
REAL ESTATE

Journal of Case Study Research™

Introduction

The Journal of Case Study Research™ is a new publication from the Center for California Real Estate (CCRE), an institute from the CALIFORNIA ASSOCIATION OF REALTORS® that is dedicated to advancing real estate knowledge. The goal of CCRE, and by extension this journal, is not only to inform the real estate community, but also to arm our 185,000 members with ideas that help them become more knowledgeable, professional, and insightful in their work as practitioners and stakeholders in the future of real estate. To fulfill this goal, CCRE regularly enlists the foremost experts on topics of pertinent interest to our industry, collaborating for impactful ideation—whether it’s engaging with our leadership, sharing expertise with policymakers and our members, or convening thought leaders for substantive discourse.

A center has an obligation to present thought-provoking and actionable ideas that can influence the direction of the industry, and the Journal of Case Study Research™ is just the latest iteration of CCRE’s efforts to serve as a resource for interesting and tactical information related to real estate. The importance of housing affordability to the industry and the state of California as a whole is reflected in the solitary theme assessed by the contributors of this journal’s first volume. We are grateful for their contributions, which highlight an area of policy, general analysis, or various tools that might advance improvements in housing affordability. The ideas range widely, but the common denominator is a solutions-based approach to ensure the state’s sizeable affordability problem is addressed from a variety of perspectives.

The case studies collected here present insightful commentary with a clear point of view, supported by research, data, and personal experience. It is our intent and hope that the Journal of Case Study Research™ starts a fruitful dialogue about solving the housing affordability crisis in California.

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BACKGROUND

The Center for California Real Estate (CCRE) is an institute founded by the CALIFORNIA ASSOCIATION OF REALTORS® (C.A.R.) dedicated to intellectual engagement in the field of real estate. Its mission is to advance industry knowledge and innovation with an emphasis on convening key experts and influence-makers. CCRE reflects C.A.R.’s increasing role in shaping the future of the industry by advancing innovative policy solutions and active dialogue with experts and industry stakeholders.

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A Note from the President

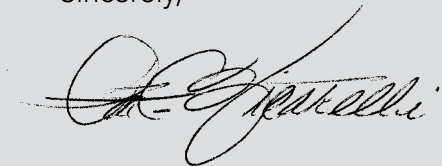
California's desirability as a place to live is undeniable, but REALTORS® see first-hand the state's economic and social problems stemming from a lack of adequate housing that is affordable, thereby denying working families the opportunity to pursue and achieve the American dream of homeownership. Our industry's professionals work tirelessly on behalf of their clients to grapple with the state's affordability issues on a personal level, but the collective voice of the CALIFORNIA ASSOCIATION OF REALTORS® (C.A.R.) and its 185,000 members is far stronger and, for more than a century, C.A.R. has led the way in making its presence felt in the legislative, legal, and consumer advocacy arenas.

This leadership role includes tackling California's pressing struggle with housing supply and affordability—an issue that greatly resonates with a membership committed to creating a path toward affordable homeownership for the state's workforce. C.A.R. continues to take an active role in monitoring and influencing legislation that addresses the planning and funding related to housing affordability. Our Housing Affordability Fund (H.A.F.) raises the resources to provide Californians financial assistance with the home-buying process, and C.A.R. formed an Affordable Workforce Housing Task Force in August 2015 to examine existing policies in California designed to expand the availability of affordable housing and to make recommendations to increase availability.

This inaugural issue of the Journal of Case Study Research™, a publication under the auspices of our institute the Center for California Real Estate, demonstrates C.A.R.'s commitment and leadership in terms of advancing industry knowledge and innovation on housing affordability. We hope our members, industry leaders, and stakeholders concerned about housing will find much to learn from the opinions and ideas featured here from key experts.

It is C.A.R. and CCRE's sincere desire to see real solutions address this issue for the betterment of the state's future. As such, we are extremely grateful to our contributors and hope you find this publication valuable and insightful.

Sincerely,



Pat "Ziggy" Zicarelli
2016 C.A.R. PRESIDENT

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Expanding Housing Supply in California: A New Framework for State Land Use Regulation

By **Carol Galante and Carolina Reid**, TURNER CENTER FOR HOUSING INNOVATION, UC BERKELEY

KEY TAKEAWAYS

- The impasse between the need to expand supply and local resistance to new development should be resolved through state action. While zoning and land use regulations have long fallen under local control, the California Legislature has repeatedly stipulated – and the courts have confirmed – that housing is an issue of statewide policy concern, and that there are reasons to limit local authority to meet public needs.
- Gov. Jerry Brown's Streamlining Affordable Housing Approvals (SAHA) proposal would address what is often cited as the primary roadblock to affordable housing developments in California: the use of the California Environmental Quality Act (CEQA) process to delay, create uneconomic approval conditions, or entirely reject multi-family infill developments.
- The state could consider adopting legislation similar to Chapter 40B in Massachusetts, which establishes a state-level appeals court for qualified projects. It uses state authority to ensure that local governments don't shirk their duty to provide housing for their workforce.

Case Study Abstract

State action is required to resolve the impasse between the need to expand supply and local resistance to new development; therefore, it is time for California to adopt a state-level framework that facilitates the production of housing in areas that align with economic, environmental, and equity goals. Under the status quo, both NIMBYs (Not In My Back Yard) and special interests use the entitlement process to prevent housing development – particularly infill, multi-family, and subsidized housing – from being built. Arguably, these are precisely the types of development we should be promoting to achieve environmental and equity goals. Improving the certainty and cost efficiency of development projects will show the state is serious about expanding supply, and "by right" legislation in particular offers a compelling approach to expanding California's supply of affordable housing. A second, complementary approach is to establish a state-level appeals process for qualified development projects.

Case Presentation

California is facing a housing affordability crisis, particularly in its coastal cities. Median rents across the state have increased 24 percent since 2000, and at the same time, median renter household incomes have declined 7 percent.¹ While there are multiple contributing factors to rising rents, it is clear that supply matters, and there is an urgent need to expand supply in equitable and environmentally sustainable ways. Over the past three decades, California has added about half the number of units needed to keep housing costs in line with the rest of the U.S., and California cities are failing to meet their Regional Housing Needs Allocation (RHNA) targets.² This gap between supply and demand has significant negative repercussions: Recent research has shown that a lack of affordable housing in cities leads to lost wages and productivity, and contributes to rising residential segregation and inequality.³

If we're serious about expanding supply, we also need to get serious about the influence local land use controls have on development. Local land use regulations and discretionary zoning fundamentally shape how much housing gets built, and at what cost.⁴ For example, in the Bay Area, each additional layer of review during the entitlement process is associated with a 4 percent increase in home prices.⁵ The current application of California Environmental Quality Act (CEQA) is also to blame; CEQA gives development opponents significant opportunities to challenge housing projects after

local governments have approved them, and can stop housing from being built or require it to be built at lower densities.⁶ Under the status quo, both NIMBYs and special interests use the entitlement process to prevent housing development – particularly infill, multi-family, and subsidized housing – from being built. Arguably, these are precisely the types of development we should be promoting to achieve environmental and equity goals.

The impasse between the need to expand supply and local resistance to new development should be resolved through state action. While zoning and land use regulations have long fallen under local control, the California Legislature has repeatedly stipulated – and the courts have confirmed – that housing is an issue of statewide policy concern, and that there are reasons to limit local authority to meet public needs. There have been numerous attempts over the years to “nip and tuck” at California’s complex legal framework of land regulations (e.g. the density bonus law, the housing element law, and CEQA reform), but by the time these revisions pass, they often lack teeth or have so many restrictions they apply only to a “mythical” project.⁷ The current approach is simply unsustainable and inequitable. It is time for California to adopt a state-level framework that facilitates the production of housing in areas that align with economic, environmental, and equity goals.

Gov. Jerry Brown’s recently introduced Streamlining Affordable Housing Approvals (SAHA) proposal

¹ California Housing Partnership Corporation (2016). *Confronting California’s Rent and Poverty Crisis: A Call for State Reinvestment in Affordable Homes*, available online at <http://chpc.net/wp-content/uploads/2016/04/State-Housing-Need-2016.pdf>.

² California Legislative Analyst’s Office (2015). *California’s High Housing Costs: Causes and Consequences*. Sacramento, CA: Legislative Analyst’s Office.

³ Hsieh, C.-T., & Moretti, E. (2015). *Why Do Cities Matter? Local Growth and Aggregate Growth*. National Bureau of Economic Research Working Paper 21154; Lens, M. C., & Monkkonen, P. (2016). “Do Strict Land Use Regulations Make Metropolitan Areas More Segregated by Income?” *Journal of the American Planning Association*, 82(1), 6–21; Ganong, P. & Shoag D. (2015). *Why Has Regional Income Convergence in the U.S. Declined?* Harvard Kennedy School Working Paper RWP12-028.

⁴ Glaeser, E. & Gyourko, J. (2003). *The Impact of Building Restrictions on Housing Affordability*. *Economic Policy Review* 9 (2): 21-39; Gyourko, J. & Molloy, R. (2015). *Regulation and Housing Supply*. in Duranton, Gilles, J. Vernon Henderson, and William C. Strange eds., *Handbook of Regional and Urban Economics*. Volume 5B. *Handbook of Regional and Urban Economics*. Amsterdam; San Diego and Oxford: Elsevier Science; Quigley, J. & Raphael, S. (2005). *Regulation and the High Cost of Housing in California*. *The American Economic Review* 95 (2): 323–328.

⁵ California Legislative Analyst’s Office. (2015). *California’s High Housing Costs: Causes and Consequences*. Sacramento, CA: Legislative Analyst’s Office.

⁶ J. Hernandez et al. (2015). *In the Name of the Environment: Litigation Abuse Under CEQA*. San Francisco, CA: Holland & Knight.

⁷ J. Hernandez et al. (2015). *In the Name of the Environment: Litigation Abuse Under CEQA*. San Francisco, CA: Holland & Knight, p. 82.

represents an important effort in this direction, and seeks to balance local land use controls with the broader goal of expanding the supply of housing. Meanwhile, the state could also consider adopting legislation similar to Chapter 40B in Massachusetts, which establishes a state-level appeals court for qualified projects. These two approaches are not either/or—they share common goals and are complementary in many ways. (See table on page 7) Both use state authority to ensure that local governments don't shirk their duty to provide housing for their workforce. Also, both apply solely to projects that expand the supply of housing for lower-income households, as well as reduce permitting timelines to lower the costs of development. In each approach, however, these shared goals are achieved through different administrative mechanisms.

Gov. Jerry Brown's SAHA proposal was included in the May 2016 budget and is currently under deliberation. The proposal recognizes that funding for affordable housing will go further if complemented by a more cost efficient and predictable land use system. In effect, SAHA fast-tracks eligible housing projects by making local design review of eligible projects "ministerial" rather than discretionary. Eligible projects would

be approved "by right," which would also mean that CEQA wouldn't apply. The proposal therefore addresses what is often cited as the primary roadblock to affordable housing developments in California: the use of the CEQA process to delay, create uneconomic approval conditions, or entirely reject multi-family infill developments.

However, the proposal also places limits on which developments would qualify for "by right" approval. Importantly, it restricts "by right" development to sites that localities have already planned and zoned for multi-family residential housing, meaning that localities still have the underlying right to determine general plan, zoning, height, and density requirements. In addition, it is limited to urbanized, infill sites reflecting the priority the governor has placed on aligning land use with transportation to achieve climate change goals.

We think "by right" legislation offers a compelling approach to expanding California's supply of affordable housing. A second, complementary approach is to establish a state-level appeals process for qualified development projects. Massachusetts Chapter 40B, passed in 1969, is often pointed to as model state legislation in this area, given its effectiveness at expanding affordable



POLICY AREA	STREAMLINING AFFORDABLE HOUSING APPROVALS (SAHA)	THE MASSACHUSETTS COMPREHENSIVE PERMIT ACT (CHAPTER 40B)
Affordability	<p>For developments within a transit priority area: at least 10 percent of total units affordable to low-income households or at least 5 percent allocated to very-low income</p> <p>For developments outside of a transit priority area: at least 20 percent of total units affordable to individuals with 80 percent or less of area median income (AMI)</p>	<p>25 percent of units must be affordable to families earning less than 80 percent of the area median income</p> <p>Proposed development must receive funding under a state or federal housing program (e.g. LIHTC)</p> <p>Regulatory Agreement</p>
Zoning	<p>Limits production to locations and densities that have already been approved by local governments in general plans and zoning codes</p> <p>Development is located on a site that is immediately adjacent to parcels that are developed with urban uses</p>	<p>Applies to areas <i>not</i> already zoned for multi-family housing</p>
Environmental Review	<p>"By right" projects are subject to "ministerial" actions since zoning and general plan had CEQA review; no added CEQA review</p>	<p>Developers must abide by the Massachusetts Environmental Protection Act (MEPA)</p>
Process Timeframe	<p>Design review of the development shall not exceed 90 days from the submittal of the development</p>	<p>Public hearings must start within 30 days of the application, which can last up to 6 months. After ending the public hearing, the Zoning Board of Appeals (ZBA) must issue a decision within 40 days</p>
Profits	<p>No developer profit caps</p>	<p>Developer must agree to cap profits to a maximum of 20 percent in for-sale developments and 10 percent per year for rental developments</p>
Review	<p>Developers must opt in to the new law with a written request to the local government stating that they intend to utilize the benefits of the new law. If the development is compliant, the city is obligated to comply and permit the project ministerially</p> <p>Failure to comply would result in a writ mandate issued by the court, ordering the city to comply</p>	<p>If the ZBA denies an application or approves it with conditions that make the project "uneconomic," developers have the right to appeal to a state-level administrative, quasi-judicial body, the Housing Appeals Committee (HAC)</p> <p>HAC has the authority to overturn a local ruling unless the zoning board can prove that there is a "valid health, safety, environmental, design, open space, or other local concern... [which] outweighs regional housing need"</p>
Exemptions	<p>No exemptions</p>	<p>Municipalities are exempt if they have at least 10 percent of their housing stock affordable to households earning below 80 percent of AMI, or are making progress towards those goals through an approved Housing Production Plan (HPP)</p>

housing in both urban and suburban localities without any documented negative impacts on local infrastructure or property values.⁸ Other states, such as Connecticut, Rhode Island, and Illinois have adopted similar approaches with success.

So what exactly is Chapter 40B and what does it do? Fundamentally, it is a broader, more comprehensive approach to the same challenges SAHA is tackling. Chapter 40B applies to all sites, regardless of underlying zoning, and streamlines the number of project reviews by instituting a process for developers to apply for a comprehensive permit for qualified affordable housing projects. In addition, in jurisdictions that have not met their fair share of affordable housing, the developers have the right to appeal to a state-level Housing Appeals Committee (HAC) if the locality denies the application or approves the development with conditions that make it “uneconomic.” Municipalities that are meeting or exceeding their housing production targets and fair share housing goals are rewarded with exemption from this process.

SAHA and application of Chapter 40B in California are promising solutions, but we know neither will solve all of California’s housing needs. Addressing the state’s lack of affordable housing will require significant public funding to provide for the most vulnerable populations. However, given limited resources, it is vital that we use such funding more effectively. Both SAHA and Chapter 40B do so by helping to improve the certainty and cost efficiency of development projects. Ultimately, implementing either, or perhaps a combination of both approaches, will be necessary to meaningfully expand the supply of housing for California’s families. ■

⁸Citizens’ Housing and Planning Association, “Chapter 40B: The State’s Affordable Housing Law,” January 2014, <http://www.chapa.org/sites/default/files/40%20B%20fact%20sheet.pdf>. Cowan, Spencer M. “Anti-Snob Land Use Laws, Suburban Exclusion, and Housing Opportunity.” *Journal of Urban Affairs* 28, no. 3 (June 1, 2006): 295–313. Lindsay Koshgarian, Alan Clayton-Matthews, and Carrie Bernstein, “Economic Contributions of Housing Permitted through Chapter 40B: Economic and Employment Linkages in the Massachusetts Economy from 2000-2010” (UMass Donahue Institute, September 2010). Alexandra DeGenova et al., “On the Ground: 40B Developments Before and After” (Tufts University, May 1, 2009). David J. Ritchay and Zoe R. Weinrobe, “Fear and Loathing in Massachusetts: Chapter 40B, Community Opposition, and Residential Property Value” (Master in City Planning, Massachusetts Institute of Technology, 2004).

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Carolina Reid is an Assistant Professor in the Department of City and Regional Planning and the Faculty Research Advisor for the Turner Center for Housing Innovation. She specializes in housing and community development, with a specific focus on access to credit, homeownership, and wealth inequality. She brings nearly two decades of applied work experience to her research and teaching.

A Housing Incentive That Actually Works

By Adam Christian, HDR, INC.

KEY TAKEAWAYS

- Under a 2001 Jobs Housing Balance Incentive Grant Program (JHB), modest grants awarded to California cities in exchange for the entitlement of additional housing units showed significant potential to accelerate residential construction activity and make meaningful inroads into the state's cumulative housing supply shortage of 800,000 units.
- Direct cash payments may be more effective than other regulatory incentives because they counteract the fiscal impacts of Proposition 13, which caps annual property tax increases and deprives cities of the ability to keep pace with the increasing cost of providing services to residents.
- Building upon the tiered incentives offered under the 2001 pilot, an updated JHB program could micro-target areas at the Census tract-level to encourage the permitting of additional housing where it is needed most.

Case Study Abstract

Many California cities, especially those in coastal areas, are reluctant to approve new housing for multiple reasons. The Jobs Housing Balance Incentive Grant Program (JHB), funded on a pilot basis for one year in 2001 by the Department of Housing and Community Development (HCD), provided modest financial incentives to California cities that permitted more housing compared to their historical averages. A follow-up HCD report issued in 2006 showed that the award of \$25 million in JHB grants resulted in nearly 21,000 additional housing units being built by a variety of coastal and inland communities. The JHB per-unit cost of \$1,500 is a fraction of the \$100,000+ per-unit cost of conventional affordable housing subsidies offered by various state programs since 2001. The success of the JHB pilot program indicates that direct cash payments to cities may be a cost-effective policy option that can accelerate the state's housing production in the near term, while tougher, long-term policy fixes are worked out. The JHB program deserves to be resurrected and funded on an ongoing basis.

Case Presentation

Editor's Note: A version of this article first appeared in the California Planning and Development Report (CP-DR).

To restore some semblance of a balanced housing market in California's major urbanized areas, most experts agree that an estimated 180,000 to 210,000 additional units would be required in Los Angeles County, and 170,000 additional units in the Bay Area.¹ In a well functioning market, this kind of severe shortage would make new home production a foregone conclusion.

Alas, we are not living in a well-functioning market, but a tangled regulatory web in which a combination of NIMBYism, environmentalism, and the fiscalization of land use wrought by Proposition 13 makes many local governments reluctant to approve new housing.

Among the key upstream challenges in the housing supply pipeline is the lack of incentive for local governments to achieve their Regional Housing Need Allocations (RHNA), the amount of new housing that cities would need to build to accommodate anticipated population growth. Currently, there are no penalties for non-compliance with RHNA targets.

In the absence of penalties, one logical solution would be to reward cities that achieve their RHNA targets. It turns out that the state experimented with a similar approach through a pilot program launched in 2001.

Administered by the Department of Housing and Community Development (HCD), the Jobs Housing Balance Incentive Grant Program (JHB) provided modest incentives to jurisdictions that voluntarily increased their permitting activity by at least 12 percent over a baseline average from the previous 36-month period. For example, if an average of 1,000 units had been permitted annually over the prior 36 months, a given city that issued permits for at least 1,120 units during the pilot period qualified for incentives.

The pilot produced near-term, cost-effective results. A final report on the JHB Program, issued in 2006 to the state legislature, estimated that participating cities permitted an additional 24,624 units of housing in 2001 compared to their rolling three-year average. Eighty-six percent, or just over 21,000, of those permitted housing units had been built and occupied five years later. Critically, many coastal communities – where housing is more expensive as a result of chronic housing underproduction – permitted more housing as a result of the JHB program.

The per-unit grant incentives were relatively low—ranging from \$500 to \$1,300 per unit (\$670 to \$1,740 in 2015 dollars) with high-density employment counties receiving higher per-unit incentives to encourage more housing near job centers. The total award pool was \$25 million; the largest award of \$3.5 million went to the city of Los Angeles. The JHB program allowed award recipients to spend the funds on new housing-related infrastructure and amenities, creating a virtuous cycle of investment in growing neighborhoods.

The JHB program's per-unit incentives should be viewed in the context of both the current depth of the state's housing need and the relative effectiveness of other housing subsidy programs:

- Proposition 46 of 2002 and Proposition 1C of 2006 together provided \$4.95 billion for the construction, rehabilitation, and preservation of 57,220 affordable apartments, at a cost of over \$86,000 per unit.
- Prior to their elimination in 2011, community redevelopment agencies set aside approximately \$1.02 billion per year for affordable housing, but rarely spent all of their allocated funds. From FY 2001 to FY 2008, 63,200 affordable units were constructed statewide at a cost of \$4.57 billion, or an average of \$73,200 per unit.²
- The Affordable Housing and Sustainable Communities (AHSC) program spent \$122 million in 2015 to subsidize the construction of

¹ Christopher Thornberg, "Why affordable housing is now a middle-class crisis in California," Los Angeles Daily News, January 14, 2016.

PROGRAM	AFFORDABLE UNITS BUILT OR REHABILITATED	AVERAGE SUBSIDY PER UNIT
Proposition 46 (2002), Proposition 1C (2006)	57,220	\$86,000
Community redevelopment agencies (2001-2008)	63,200	\$73,200
Affordable Housing and Sustainable Communities (AHSC) Program (2015)	1,924	\$63,400
Federal Low Income Housing Tax Credit (LIHTC) Program (annual average)	7,000	\$165,000
	MARKET-RATE UNITS CONSTRUCTED	
Jobs Housing Balance (JHB) Grant Incentive Program (2001)	21,201	\$1,180

1,924 units statewide, at an approximate cost of \$63,400 per unit.

- The federal Low Income Housing Tax Credit (LIHTC) program has produced around 7,000 new rental units annually, at an average cost of \$165,000 per unit in coastal communities.

Since subsidized affordable housing projects often receive funding from multiple programs, the total per-unit subsidy is likely higher than the amount shown for any single program. By comparison, the average cost per unit for the JHB program was around \$1,180 (\$1,580 in 2015 dollars) and less than the state incentive on some electric cars.

Let's address two obvious arguments with these comparisons:

The HCD follow-up report can't quantify how many of these units would have been permitted anyway due to the real estate upcycle that was occurring in 2001, and how many of these permits were directly attributable to the incentives.

True, but even if only a fraction of the total unit production were directly attributable to the incentives, the JHB program is still dramatically more cost-effective than its next closest peer. It is also more transparent and simpler to administer.

This comparison is a case of "apples and oranges:" The cost of permitting a unit of market-rate housing and the cost of producing a unit of affordable housing are not directly comparable or equivalent in their social impact.

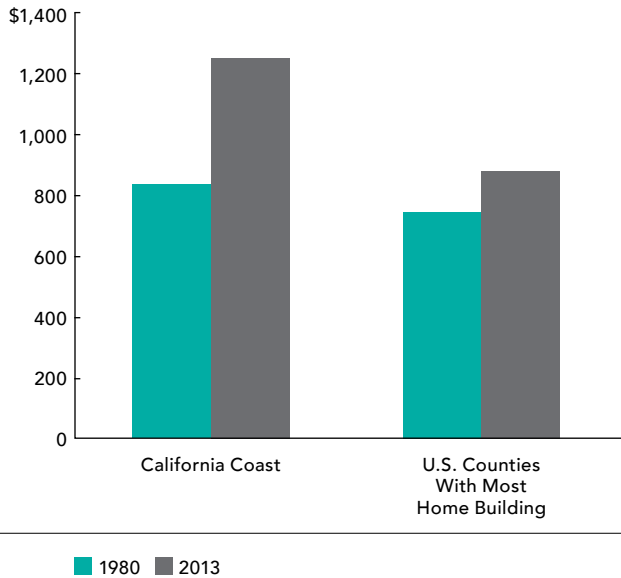
A Legislative Analyst Office (LAO) report released in February 2016 provides compelling evidence to the contrary. Increased production of market-rate housing would have broad-based affordability benefits for households at all income levels. Strikingly, the LAO report found that cities with abundant market-rate housing production were far less likely to displace low-income residents than cities with slow growth policies.³ While targeted subsidies for very low- and low-income households will continue to be both morally and economically

² Redevelopment Agencies in California: History, Benefits, Excesses and Closure," U.S. Department of HUD Office of Policy Development and Research, Economic Market Analysis Working Paper No. EMAD-2014-01, January 2014, accessed at https://www.huduser.gov/portal/publications/redevelopment_whitepaper.pdf.

³ California Legislative Analyst Office, "Perspectives on Helping Low Income Californians Afford Housing," Report 3345, January 2016, accessed at <http://www.lao.ca.gov/Publications/Report/3345>.

PLACES WITH MORE BUILDING SAW SLOWER GROWTH IN RENTS FOR POOR HOUSEHOLDS

Rents Paid by Low-Income Households in Urban Counties (In 2013 Dollars)



Source: Legislative Analyst's Office

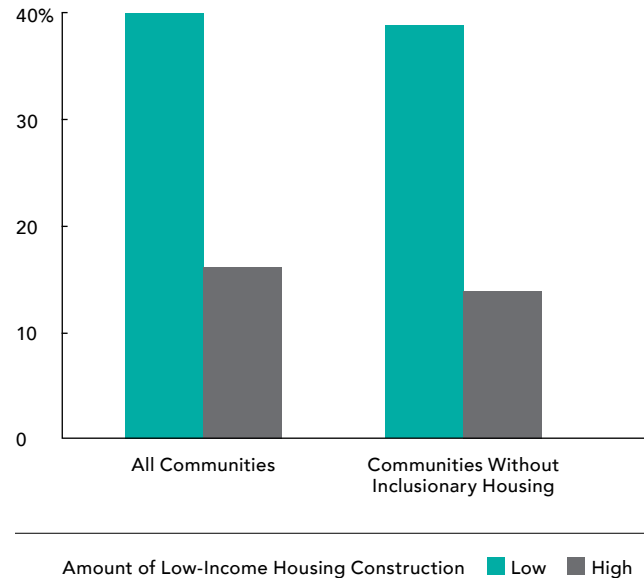
necessary, everyone wins with an increase in the overall supply of housing.

The JHB Program shows that the reluctance of local governments to approve more housing, at least in the near term, may be most easily overcome with cold hard cash. In an era of dwindling state and federal assistance to cities, many communities – whether coastal or inland, affluent or low-resource – may be even more motivated now than in 2001 to pursue every discretionary dollar out there.

In resuscitating the JHB Program, the state wouldn't have to reinvent the wheel, as there is already a statutory mechanism in place; it would just need a dedicated, sustainable funding source. While

BUILDING MARKET-RATE HOUSING APPEARS TO REDUCE DISPLACEMENT

Percent of Low-Income Bay Area Census Tracts That Experienced Displacement Between 2000 and 2013



many sources could be considered, there would be a strong policy justification for using a portion of cap-and-trade funds for this purpose. The construction of new housing in job-rich areas would directly support shorter commutes, a reduction in household Vehicle-Miles Traveled (VMT), and hence a decrease in greenhouse gas emissions.

Ideally, cities should not have to be bribed into approving new housing. But we are not living in an ideal world. Given the urgency of California's affordability crisis, a program with the potential to produce near-term, cost-effective results deserves to be resurrected from the state's policy graveyard. ■

Adam Christian is a senior consultant in infrastructure funding and finance at HDR, Inc.

California's Housing Policies Need Real Reform

By Christopher Thornberg, Ph.D, BEACON ECONOMICS, LLC

KEY TAKEAWAYS

- The reason housing is so expensive at all levels in the state is the lack of new housing construction, and while California has a greater than average population growth rate, it has accounted for less than 9 percent of new residential housing unit permits over the past 20 years.
- California is failing to acknowledge the general shortage of housing. Instead, it is only offering fixes for low-income housing, such as rent control or affordable housing mandates for new construction. But these programs will not work in an environment with a broader housing shortage.
- Inclusionary policies ultimately represent a tax on one source of supply (market rate) to supplement another source (affordable housing). While such programs may help some low-income families, it ultimately comes at the expense of raising housing costs for middle- and higher-income families.

Case Study Abstract

California is failing to acknowledge its general shortage of housing because the state is not addressing the source of its housing problem: Past policies that are creating barriers that prevent the state's housing supply from coming online in the first place. Despite the fact that empirical studies have shown that inclusionary housing programs drive up the cost of normal housing, and deliver only a small impact on the overall housing supply, reliance on such programs means the state is pushing "solutions" that will end up doing little good and ultimately may end up doing even more harm. These programs will not work in an environment with a broader housing shortage.

Case Presentation

California’s housing affordability problem is intensifying and may well slow the rapid growth the economy has been enjoying over the last few years. Unfortunately, there is either an unwillingness or inability to consider the full scope of the problem and the root causes—focusing instead only on one aspect of the issue. The state is pushing ‘solutions’ that will end up doing little good and ultimately may end up doing even more harm.

Start with the definition of the problem. The conversation coming out of Sacramento seems to always refer to the issue as a crisis of affordability. The focus tends to be almost exclusively on lower-income families in rental housing. There is little doubt that these families are having a tough time in the state. Start with the standard metric that families should not spend over 30 percent of their income on housing. It turns out that over 90 percent of lower-income families in California fall into this category of spending more than that percentage. But then housing is a problem for low-income families across the nation where the comparable figure is 83 percent. In other words, this conversation is less about local housing and more about the national problem of poverty and income inequality.

What makes the California housing issue even more serious is that the high-cost factor hits all residents in the state—not just low-income families. For

example, 53 percent of California’s middle-income renting households are housing cost burdened—compared to 26 percent in the nation. For those who buy homes, 46.4 percent are cost constrained compared to a national average of 26.6 percent.

While the housing cost burden on middle- and higher-income families may seem like a less pressing social issue, the economic impact is anything but small. When families have to spend more on housing, they spend less on other things, hurting the economy overall. Businesses in the state that are competing nationally or globally for the best talent find themselves in a weaker bargaining position because of the housing situation. Many families – often representing the mid-skilled workers who are the backbone of modern industry – choose simply to move out of state in order to afford a better standard of living—leaving California with labor shortages in many areas of the economy.

The reason housing is so expensive at all levels in the state is the lack of new housing construction. While California is home to over 13 percent of the nation’s population and has greater than average population growth rate, it has accounted for less than 9 percent of new residential housing unit permits over the past 20 years. As a result, the state has one of the lowest housing vacancy rates and one of the highest overcrowded housing rates in the nation.

SHARE OF HOUSEHOLDS SPENDING MORE THAN 30 PERCENT OF INCOME ON HOUSING COSTS

INCOME LEVEL	U.S.	CALIFORNIA
	OWN	
Up to \$34,999	58.8%	68.7%
\$35,000 to \$74,999	26.6%	46.4%
Over \$75,000	7.5%	16.3%
	RENT	
Up to \$34,999	83.1%	91.0%
\$35,000 to \$74,999	31.5%	53.1%
Over \$75,000	5.7%	10.5%

CALIFORNIA ASSOCIATION OF REALTORS® TRADITIONAL HOUSING AFFORDABILITY INDEX
FIRST QUARTER 2016

C.A.R. REGION	HOUSING AFFORDABILITY INDEX	MEDIAN HOME PRICE	MONTHLY PAYMENT INCLUDING TAXES & INSURANCE	MINIMUM QUALIFYING INCOME
Calif. Single-Family Home	34	\$465,280	\$2,314	\$ 92,571
Calif. Condo/Townhomes	41	\$389,910	\$1,939	\$ 77,575
Los Angeles Metropolitan Area	35	\$436,850	\$2,173	\$ 86,015
Inland Empire	48	\$297,850	\$1,481	\$ 59,259
San Francisco Bay Area	27	\$723,060	\$3,596	\$143,858
United States	60	\$217,600	\$1,082	\$ 43,293

Source: CALIFORNIA ASSOCIATION OF REALTORS®

If we applied national averages for housing vacancies and residents-per-household to California, it would suggest that the state is short 700,000 to 800,000 units overall. And the problem is getting worse—in the last two years the state has added over four new residents for each new building permit, in a place that averages 2.5 people per household.

This lack of new construction can be linked to many global factors. These include issues such as poor local zoning ordinances; CEQA (California Environmental Quality Act), which is used and abused by many special interests to delay and shrink housing developments; and Proposition 13, which limits the financial value of housing for local governments—an issue they understandably deal with by restricting such growth through fees and zoning.

California is failing to acknowledge the general shortage of housing. Instead, it is only offering fixes for low-income housing, such as rent control or affordable housing mandates for new construction. But these programs will not work in an environment with a broader housing shortage. Take the new state tax on property transfers that was proposed (and

ultimately vetoed) to fund affordable units. This program would have produced 10,000 units over five years—not even enough to cover the growing shortage.

Some ideas are not just insufficient but can actually do harm. Take, for example, rent control. Beacon Economics recently did a study for the California Apartment Association that found while rent control did hold rents down in specific neighborhoods, it completely failed to help low-income households. Instead, middle-income households filled these limited spaces, thereby pushing low-income families out of the local supply. Another impact was to reduce the stock of available rental units as landlords naturally worked to find other ways to extract the full value out of their holdings, such as condominium conversions. These are not new results—they simply add to an existing wealth of studies that show rent control simply does not work.

Also being considered in California are affordable housing mandates. Such rules require developers to set aside a certain number of units for below-market rate housing, or pay a fee into an affordable housing fund. On its surface, this seems like a program that

could alleviate the strains on lower-income households. Yet, as with rent control, the actual results often turn out to be just the opposite.

Remember that the issue in California is a lack of overall supply. There is no free lunch. Inclusionary policies ultimately represent a tax on one source of supply (market rate) to supplement another source (affordable housing). While such programs may help some low-income families, it ultimately comes at the expense of raising housing costs for middle and higher-income families—who are also feeling the strain of expensive housing. It's like rearranging the deck chairs on the Titanic.

And of course, such housing programs must be supported with complex regulations and an expensive bureaucracy. Below market-rate units can only remain so with strict controls by local authorities and extensive means testing to make sure the units are being delivered to the right constituents. Otherwise, you risk the breakdown that occurs as with rent control situations. All of these problems will serve to diminish the overall housing stock and add more red tape to an already burdensome process for land developers.

This isn't idle rhetoric. Many empirical studies have shown that inclusionary housing programs drive up the cost of normal housing, and deliver only a small impact on the overall housing supply. This shouldn't be a surprise—you can't tax supply to reduce a supply shortage.

In general, the government should not kid itself into thinking this problem can be fixed with a new policy. The only way to deal with such a large shortfall is to go to the source of the problem—past policies that are creating barriers that prevent the state's housing supply from coming online in the first place. California leaders need to address zoning rules, amend Prop. 13, and enact major CEQA reform. Unfortunately, as with so many issues, California seems more inclined to go for cheap political wins with few benefits rather than take on the difficult task of providing real reform to a housing market that so desperately needs it. ■

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Since 2006, Thornberg has served on the advisory board of the Wall Street hedge fund Paulson & Co., Inc. In 2015, he was named to California State Treasurer John Chiang's Council of Economic Advisors. He is on the boards of the Los Angeles Area Chamber of Commerce, the Central City Association (Los Angeles), the Asian Real Estate Association of America, and America's Edge, a nonprofit organization focused on strengthening the economy through public investments in youth and education.

Prior to launching Beacon, he was an economist with UCLA's Anderson Forecast where he regularly authored economic outlooks for California, Los Angeles, and the East Bay. Thornberg holds a Ph.D. in Business Economics from the Anderson School at UCLA, and a B.S. degree in Business Administration from the State University of New York at Buffalo.

New Tool Could TILT Property Owners in Favor of Housing Development

By **Edward Segal**, FORMER CEO OF THE BEVERLY HILLS/GREATER LOS ANGELES ASSOCIATION OF REALTORS® AND THE MARIN ASSOCIATION OF REALTORS®

KEY TAKEAWAYS

- Property owners often use a variety of strategies and tactics to block affordable housing plans and proposals.
- Tax Increment Local Transfers (TILTs) could become a novel way to address the country's housing crisis by helping to reduce opposition to and generate support for the construction of new and affordable housing developments.
- TILTs could be an effective lobbying tool for affordable housing advocates. If enough residents participate in the innovative tax rebate program, it could place additional pressure on elected officials to support housing initiatives.
- There's no reason why TILTs would not work in California. REALTORS® and their local associations should consider asking local lawmakers to be among the first in the country to pass and implement TILTs in their communities.

Case Study Abstract

Proposals to build affordable housing are often met with fierce opposition by property owners in local and nearby neighborhoods. David Schleicher, Associate Professor of Law at Yale University, has proposed a novel way to help reduce that resistance by offering an incentive to property owners. The incentive would take the form of temporary tax rebates funded by the new tax revenue generated by the housing development.

Dubbed by Schleicher as Tax Increment Local Transfers (TILTs), the incentive builds on the successful practice of international trade deals that can provide benefits and concessions to opponents in exchange for their support of agreements. It also borrows from the tactics of municipal governments who, in an effort to convince communities to accept new development, offer various enticements to help win them over.

Key provisions of TILTs – such as the size and duration of the tax rebates and how property owners could qualify to receive them – would be up to local governments to decide.

Case Presentation

Efforts to help solve California’s decades-long shortage of affordable housing have been stymied by staunch (and sometimes strident) opposition of neighbors who do not want affordable housing projects or any new development to be built near them. Three frequently used acronyms symbolize the resistance by individuals who are loath to allow new development of any kind in their midst: NIMBY (Not In My Back Yard), BANANA (Build Absolutely Nothing Anywhere Near Anybody), and LULU (Locally Unaccepted Land Use).

OPPOSITION FOLLOWS A FAMILIAR PATTERN

Over the course of the 10 years that I served as the CEO and Government Affairs Director of the Marin Association of REALTORS® in Northern California, I saw firsthand how vocal and persistent opponents to housing projects could be. Their tactics would often include writing news releases, letters to the editor, and op-eds; soliciting support from elected officials; testifying at public hearings; calling radio talk shows; organizing and publicizing town hall meetings; conducting petition drives; placing postings on social media sites; establishing coalitions of like-minded citizens; and requesting that the REALTOR® association take a stand. The association could be caught in the middle of the debates as it sought on the one hand to defend private property rights while advocating for affordable housing on the other.

Resistance was predictable, whether the proposals were for a small Habitat for Humanity project, a row of affordable housing units, proposed regional zoning changes, suggested modifications to countywide housing elements, or plans for large residential tracts with carve-outs for below market-rate housing.

A DIFFERENT APPROACH

A novel approach has been put forth from the world of academia that could become a new tool for affordable housing advocates in California. David Schleicher is an Associate Professor of Law at Yale Law School and an expert in land use, local government law, and urban development. In an article he wrote for the Yale Law Journal that was published in 2013, Schleicher proposed that local governments offer property owners a financial incentive not to oppose new development in their neighborhoods.

The incentive would take the form of a multi-year rebate of a portion of that individual’s property taxes, such as 25 percent. The rebate would be paid from the increased tax revenues that would be generated after the new development is completed. Schleicher dubbed this innovative approach Tax Increment Local Transfers, or TILTs.

Schleicher posits that the rebates would give property owners an incentive not to oppose affordable housing projects or new development. “The money



(for the rebates) would be tied to property taxes created by the new project for a number of years, starting from the date of the (project's) proposal. This would give potential recipients an incentive to not slow down the project," he noted.

Indeed, this approach could help encourage support throughout the community for a range of projects that might otherwise be blocked. If enough people agree to take the rebates, that alone could place additional pressure on reluctant elected officials.

Schleicher's idea builds on other strategies and tactics that have been used to placate NIMBYism, including impact fees and privately-negotiated concessions from developers that help benefit the community, such as open spaces, parks, or roads.

TILTs would have no impact on the cost of construction, housing, or rents. Indeed, because developers would not have to spend money to placate local opposition to their projects, the use of TILTs could help make housing cheaper.

Schleicher has suggested that TILTs would be similar to some international trade deals, such as trade adjustment assistance, which "takes money that the general public gets from something that is generally positive, and uses some of the gains to buy off local opposition."

However, to help put the TILT concept to work in their communities, local governments would have to consider, address, and flesh out several important details, particularly the following:

- **Proximity:** How close to new developments do property owners need to live in order to qualify for the rebate?
- **Density:** Should people who live in sparsely populated areas adjacent to proposed housing projects be offered rebates?
- **Amount:** How large of a rebate would they be entitled to?
- **Duration:** How long would the rebate last?
- **Impact:** How would the tax rebate affect a government's budget and revenue projections?
- **Paperwork:** What documents would the property owners have to sign?

NOT A PERFECT SOLUTION

In his article for the Yale Law Review, Schleicher acknowledges that TILTs would have their limitations. "While TILT payments probably would not be sufficient to quell opposition among the most affected residents – a tax rebate is not likely to change the mind of someone who owns property right next to a proposed skyscraper that would ruin her view – they would limit the ability of those residents to garner broader support in the neighborhood," he wrote.

In an interview for the Journal of Case Study Research™, Schleicher said he came up with the idea for TILTs as part of several ways to help address the country's housing crisis. "Many of our biggest and richest cities restrict development excessively. In the face of high-demand places like San Francisco or New York, restrictive zoning has meant huge price increases. This has become a national economic problem," Schleicher said.

He added, "The politics of land use in rich regions and in big cities are biased against development."

Schleicher went on to say in the interview that, "The TILT proposal is meant to provide local governments where there is a great deal of housing need (and high prices) – but massive opposition to housing construction – a tool for overcoming that opposition."

Other than laying out the basic concept of TILTs, the professor has not fleshed out a detailed explanation of the tactics or offered any statutory language for policymakers to consider. He said he is content to put forth his proposal as an idea that could work.

Although TILTs have received favorable coverage in the media, his unique approach has not yet been implemented. "Cities have offered all sorts of goodies to neighborhoods to accept new development – look at what New York City is offering as part of the East New York rezoning – but no one has actually adopted anything like TILTs," he said.

PUTTING THE IDEA TO WORK

Schleicher sees no reason why TILTs would not work in California. "You should remember that the TILT

idea is not a very specific proposal, but rather is a way of approaching opposition to new projects. Homeowners near new development are not simply going to sit on their hands, so we need to change development politics—understanding that this is the case. TILTs are a way to approach payoffs that does not result in a tax on development,” he said.

He added, “The only reason to give such rebates is to lessen opposition, so the amount should be driven by the extent of the opposition. The two biggest problems with implementation are [to] determine who should get the rebates – property owners on the same block or blocks or more distant ones – and how big (and for how long) they should be given. [...] I think experimentation is necessary to figure out exactly who should get how much, but the amount should be enough that it provides incentives not to oppose projects, and small enough that the city as a whole still gains from the project.”

When leading the Marin Association of REALTORS®, I used a variety of strategies and tactics to advocate the association’s affordable housing-related policy positions and activities. Looking back, I wish that TILTs had been in place as a way to help tip the balance in our favor.

Today, TILTs have the potential to help REALTORS® and their local associations gain the upper hand in the affordable housing arena. Asking their elected officials to be among the first in the country to adopt and implement TILTs may be the next step to helping solve California’s housing shortage. ■

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Segal is the former marketing strategies columnist for the Wall Street Journal’s StartUpJournal.com and author of two PR handbooks, including *Getting Your 15 Minutes of Fame* (Wiley) and *Profit by Publicity* (iUniverse). His bylined articles on PR-related topics have been published by the National Association of REALTORS®, seven state REALTOR® associations, and the American Society of Association Executives.

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Innovative Investment Approaches for Preserving California's Existing Workforce Apartments

By **Stockton Williams**, URBAN LAND INSTITUTE TERWILLIGER CENTER FOR HOUSING

KEY TAKEAWAYS

- Even as California needs to build more market rate and affordable housing units, industry leaders must also focus on preserving the existing supply of low-cost workforce apartments.
- Preservation is more cost effective and environmentally sustainable than new construction and can deliver competitive financial returns to investors.
- More investors – public, private, and philanthropic – should step up to the opportunity to preserve California's workforce housing and fill this need.

Case Study Abstract

California's existing supply of low-cost workforce apartments is critical community infrastructure that is diminishing due to market forces and expiring rent restrictions. The cost of replacing these units with new ones will far outweigh what can and should be invested today to preserve this segment of the state's housing stock. Innovative financial approaches are proving that workforce housing preservation is both a smart social and financial investment—and demonstrate the opportunity for more equity capital to meet a growing need.

Case Presentation

Most discussion and efforts to address California's rapidly worsening housing affordability needs are rightly aimed at expanding the supply of new market-rate housing and below-market or subsidized units. But it is also essential that housing industry leaders focus on "preserving" the existing supply of low-cost rental apartments. "Preserving" means making the necessary capital improvements to keep units in decent condition and ensuring that rents remain affordable to lower-income households. Socially motivated real estate firms and investors are showing this can be done while delivering significant social and financial returns.

California's existing supply of low-cost apartments is a critical segment of the state's housing stock. There are roughly 150,000 privately-owned, rent-restricted units in California that were financed with federal housing assistance of various kinds. The California Housing Partnership estimates that more than 50,000 of them may raise rents significantly over the next five years as they reach the end of their rent-restricted periods. There are also hundreds of thousands of low-cost units in multi-family properties across the state that are "naturally affordable," meaning that while they are not subject to federal rent restrictions, they are nevertheless relatively affordable to lower-income renters due to their age, limited amenities, and surrounding market conditions.

These apartments represent essential infrastructure that support almost every California community. They are where many in the state's service and blue collar workforce live—most by necessity, some by choice. Once these units fall into physical obsolescence or are "repositioned" to much higher market rate rents, they will be extremely difficult, if not impossible, to replace. In a state that knows full well tough fiscal tradeoffs, it bears reminding that preserving an existing workforce apartment costs half or less than what it would to replace it with a new one. And of course, preservation is more environmentally sustainable than new construction.

Further evidence of the smart economics of workforce housing preservation is in the remarkable recent progress of a variety of equity and debt funds

focused on this market segment in California. One example is Avanath Capital Management, based in the city of Irvine. The firm acquires and preserves properties serving residents earning 80 percent of the area median income, while paying its investors – which range from pension funds and financial institutions to foundations and family offices – an attractive 6 – 10 percent "cash on cash" (current income) return. Avanath's last two equity funds raised more than \$300 million combined. Through its property management affiliate, which manages more than 6,000 units, the firm focuses on optimizing maintenance and keeping occupancy levels near or at 100 percent. About half of Avanath's activity is in California.

Another approach is represented by the Los Angeles New Generation Fund, which was established in 2008 through a partnership of the Housing and Community Investment Department of Los Angeles, local foundations, and private lending institutions. The fund was designed to combat homelessness and reduce the housing burden on poor and working families by offering affordable housing developers early-stage financing for properties intended for low- and moderate-income residents. The fund is currently capitalized at \$75 million and has created or preserved more than 1,300 units in 14 developments.

One example is The Rosslyn Hotel in rapidly redeveloping downtown Los Angeles. The fund is enabling a gut rehabilitation of the property to LEED Silver green building standards, with ground floor retail. When complete, 184 units will be available to very low-income households, with another 70 for formerly homeless individuals.

Then there is the Housing Partnership Equity Trust, which was established in 2013 as an independently managed, shareholder-owned, for-profit corporation that acquires unsubsidized, "naturally occurring," affordable multi-family rental properties in partnership with 12 nonprofit housing developers. The Trust, currently capitalized at \$80 million, provides its investors stable, long-term dividends: Current preferred equity receives a 4.5 percent coupon and the common equity dividend is targeted to a spread above that. While the Trust is based in Washington, D.C., it has been active in California.

For example, the Trust, in collaboration with Eden Housing, Inc., acquired the 129-unit Woodside Court Apartments in Fairfield. Residents work at the nearby Travis Air Force Base, Northbay Medical Center, and the County of Solano. The property is also near parks and recreation facilities, elementary and secondary schools, and a community college.

These and other innovators have proven the case that workforce housing preservation is a viable sector for socially-motivated, return-seeking equity investment. Yet, while California's workforce housing preservation funds are generating impressive results, market forces play out much faster than mission-oriented organizations can typically move. These entities need more flexible capital in order to compete with conventional multi-family value-add investors. This is a solvable problem, especially in a state with a long history of social innovation to tackle big challenges.

The need is clear and the economic case is increasingly compelling for saving the state's workforce housing stock. Now, California pension funds, financial institutions, large foundations, and high-net worth individuals must step up and invest—before it is too late. ■

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EITC Housing Supplement Fails to Address State's Underlying Problem

By **William Chen**, CALIFORNIA BUDGET & POLICY CENTER

KEY TAKEAWAYS

- The proposed housing supplement would equal the difference between 30 percent of household income, including the EITC, and local fair market rent. Although under this proposal no household would be “cost-burdened,” the proposal would significantly increase EITC program costs.
- The supplement would not address California’s underlying problem: a severe housing shortage. Putting more money into people’s pockets without boosting production of housing, particularly affordable units, would only drive up costs further.
- Policymakers’ proposal to expand “by right” approval for multi-family housing projects with set-asides for affordable housing is a good first step in streamlining development and getting affordable housing on the market more quickly.
- Compared with market rate housing production, building subsidized housing is more than twice as effective in protecting low-income households from displacement. While seeking to streamline production, policymakers should expand subsidized housing solutions, such as the Low Income Housing Tax Credit, housing vouchers, and new initiatives like the bond under consideration to fund supportive housing programs for homeless people with mental health needs.

Case Study Abstract

Nationally, housing affordability is a growing problem, with falling homeownership rates and an increasing number of cost-burdened renters. In California, housing is particularly expensive. Dr. Peter Dreier of Occidental College proposes adding a housing subsidy to the federal Earned Income Tax Credit (EITC). This housing supplement would equal the difference between 30 percent of household income, including the EITC, and local fair market rent. Although the proposal directly addresses the definition of “cost-burdened,” the housing supplement’s simplicity makes it a rough method of addressing needs. There are administrative questions, in part concerning possible over-subsidization for certain household types. The proposed housing supplement would also significantly increase the cost of the EITC program. Most important to California’s context, though, is that the proposal would not address the state’s underlying problem: a severe housing shortage.

Case Presentation

The national homeownership rate has fallen back to where it was two decades ago, helping to drive up rental demand. Rents grew faster than inflation in 2012, 2013, and 2014, and in 2013, the number of cost-burdened renters reached a new high of 20.8 million—just under half of all renters nationwide. The U.S. Department of Housing and Urban Development (HUD) considers households paying more than 30 percent of income in housing costs to be cost burdened.

Californians face a particularly challenging housing market. The average cost of a home here has grown to two-and-a-half times the national average, and the average monthly rent in California is now 50 percent higher than the national average. At the same time, inflation-adjusted hourly wages for low-

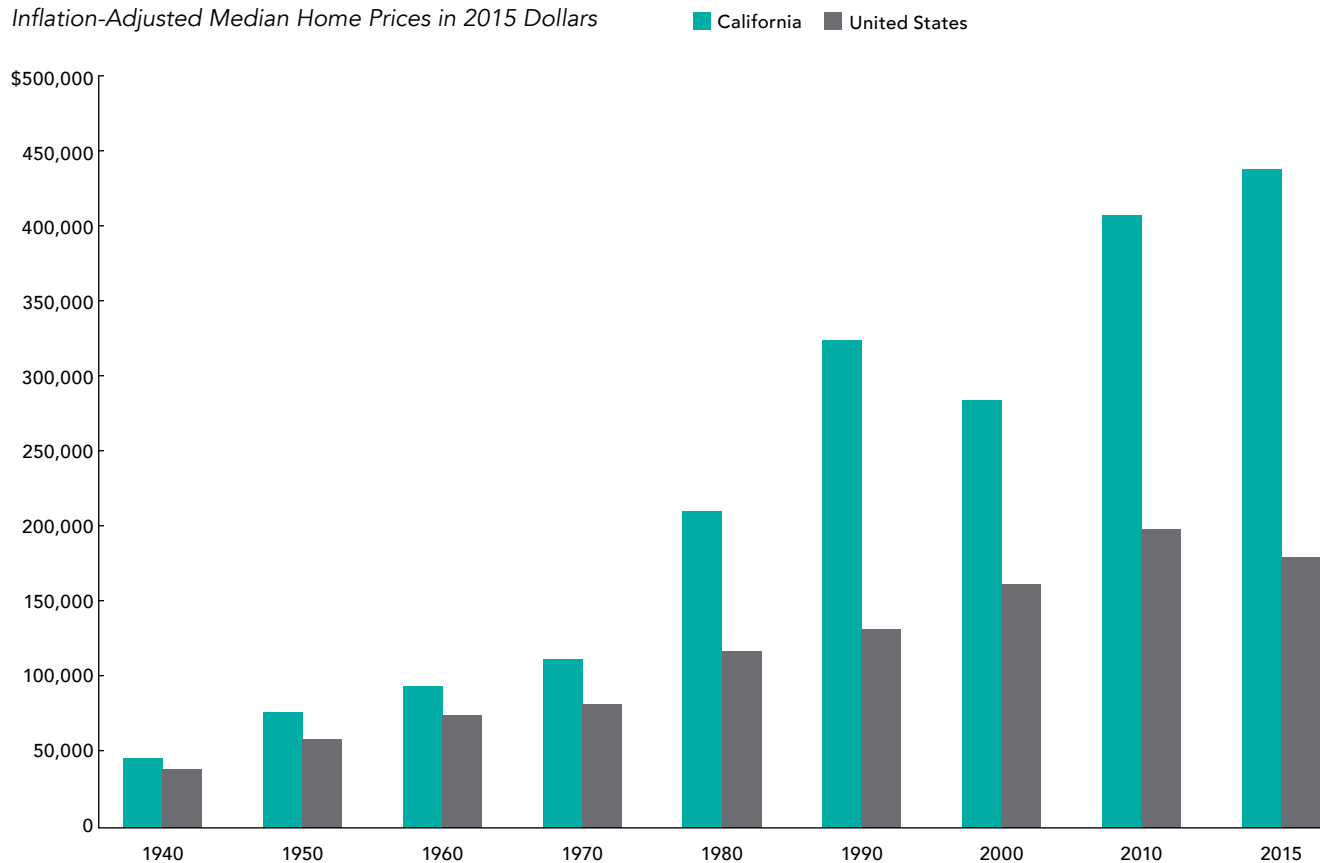
and middle-wage earners in California are below where they were in 1979.

To help address the problem of housing affordability, Peter Dreier, Chair of the Urban & Environmental Policy Department at Occidental College, proposes that a supplemental housing subsidy be added to the existing federal Earned Income Tax Credit (EITC). This housing supplement would be equal to the difference between 30 percent of household income, including the EITC, and the local fair market rent (FMR).¹ This way, no household receiving the EITC would pay more than 30 percent of its income for housing costs, at least relative to the FMR where they live.

Because it would vary according to local FMR, the housing supplement would be responsive to differences in regional housing markets. Housing

CALIFORNIA HOME PRICES HAVE GROWN MUCH FASTER THAN U.S. PRICES

Inflation-Adjusted Median Home Prices in 2015 Dollars



Source: Legislative Analyst's Office

¹ FMR is generally the 40th percentile rent for apartments in an area, defined separately for units with different numbers of bedrooms.

is far more expensive in coastal cities, such as San Francisco and Los Angeles, than in inland cities like Bakersfield and Fresno. In 2013, the average monthly rent in both Bakersfield and Fresno was just below the U.S. average of \$840, while in Los Angeles and San Francisco the average was \$1,390 and \$2,000, respectively.

Dreier's proposal does raise some administrative questions when considering its implementation. Currently, the EITC does not distinguish between homeowners and renters, so his proposal would help EITC recipients regardless of whether or not they were paying rent or mortgage payments, or already owned their home. Also, beneficiaries could be over-subsidized if, for example, someone lived alone in a two-bedroom apartment or two individuals who filed taxes separately shared an apartment. Because of its simplicity, the proposal is a rough method of addressing housing needs.

One challenge to using the EITC as a mechanism for housing assistance is that the credit arrives in a lump sum at the end of the tax year, after a household has filed its return. This is poorly structured to help a family pay rent or other ongoing expenses. Dreier highlights a Brookings Institution paper on existing advanced and periodic payment systems in other countries, which are being studied in the U.S. These might be more complicated than providing a lump sum payment at the end of the year, but they provide the benefit of increasing availability of funds throughout the year and helping families avoid taking out loans.

Another consideration is that the EITC only reaches working households. Other policies to help jobless households would still be necessary. The existing housing voucher program helps families regardless of job status. California's renter's credit only provides a very small dollar amount, and because it is a nonrefundable credit – it only benefits households earning enough to owe California income tax – it does not help those most in need.

Perhaps of more immediate political concern, however, is that the proposed housing supplement would significantly increase the cost of the EITC program. Consider, for example, a single parent with two children in Los Angeles working full-time and earning the 25th percentile annual wage of \$24,211. The housing supplement would more than triple the cash benefit they receive, from about \$4,300 for the EITC alone to about \$13,600 once the roughly \$9,300 gap between 30 percent of income (including the EITC) and FMR is filled.² A married couple in Los Angeles with each spouse working full-time at the 25th percentile wage with two children would receive a boost smaller in dollar amount due to their higher combined income, but a much larger increase as a proportion. This is because filling in the roughly \$3,300 gap between FMR and 30 percent of work income plus EITC benefit increases the total benefit received to \$3,600—almost 11 times the nearly \$330 of their federal EITC alone.

Certainly, in cities with lower housing costs than in Los Angeles, the gap to fill would be smaller, making for a lower cost for the housing supplement. Also, there is much variation in workers' situations, as not everyone works full-time or at the same wage, so the amount of subsidy needed to reach FMR would vary widely among households. But the way the proposal is structured means the value of the EITC plus housing supplement essentially starts at a region's FMR and declines as the household's earnings rise to replace the supplement.

This raises a related political consideration: The proposal weakens the work incentives underlying the EITC. Currently, EITC benefits increase as income rises, up to a plateau before decreasing again. In contrast, the *combined* benefit of EITC and the housing supplement would *only decline* as income rises.³ Although, overall income would still rise with every dollar earned as the benefits phased out. The strong political support for the EITC is due in part to the work-incenting aspect of the EITC. While some may welcome Dreier's formulation, which would directly cover housing cost burden

² I produced my estimates using the most recent wage data, updated to the first quarter of 2015, from the California Employment Development Department, and FY2016 FMR data from HUD. EITC estimates are for tax year 2015.

³ That is, starting after the first dollar earned, since the EITC only serves families with at least one job-holder.

for any working family, others would likely view the proposal as dis-incentivizing work.

Most important to California's context, though, is that the proposed housing supplement would not address the underlying problem in the state: a severe shortage of housing. The need for additional housing in California far outstrips annual production. Between 1980 and 2010, California would have had to add around 210,000 housing units each year to keep housing costs from growing faster than the national average. This is 90,000 units more than the 120,000 that California actually added each year on average. Putting more money into people's pockets without boosting production of housing, particularly affordable units, would only drive up costs further. As long as housing supply continues to fall far short of demand, housing costs in California will remain high—and unaffordable to many.

The governor and legislature's proposal to expand "by right" approval for multi-family housing proposals with set-asides for affordable housing is a good first step in streamlining the development process and getting more affordable housing on the market more quickly. Under this change to state law, housing developments that meet certain baseline requirements, including setting aside units to be affordable to low-income households, may be permitted by city or county planning staff without further approval from elected officials or discretionary approval processes.

The affordable housing criterion is important. Focusing on expanding housing supply without regard for affordability will not necessarily help lower-income families. As a recent University of California, Berkeley study found, market-rate housing construction may "eventually help lower rents decades later, [but] these units may still not be affordable to low-income households." Instead, the study found that subsidized units built with Low Income Housing Tax Credits and other federal and

state subsidies had more than double the protective effect against displacement of low-income households as did market-rate housing production.

In addition to continuing to explore how the state and localities can streamline housing development, policymakers should support subsidized housing solutions, such as the Low Income Housing Tax Credit, housing vouchers, and new initiatives like the \$2 billion bond under consideration to fund supportive housing programs for homeless people who need mental-health assistance. ■

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Assessing the Fallout from Redevelopment Agency Dissolution:

FINDINGS OF THE 2015 CALIFORNIA POST-RDA AFFORDABLE HOUSING DEVELOPER SURVEY

By **Gabriella Chiarenza**, FEDERAL RESERVE BANK OF SAN FRANCISCO

KEY TAKEAWAYS

- Local agencies are running low on financing dollars for new projects and contending with uncertainty around future funds. New construction projects are more difficult to fund without redevelopment agencies (RDAs), thereby pushing developers to focus more on acquisition and rehabilitation projects.
- As developers pursue new individual sources for affordable housing, they caution that none seem to be large enough to replace the amount of RDA funding previously available, and it is also unclear at this point how much funding these new sources will provide over time.
- Without RDA funds for site acquisition, developers note that it is very difficult for them to outbid market-rate developers, so they are more likely to be diverted to less-desirable sites that are more affordable in land costs but end up adding costs in site readiness and remediation.
- Developers emphasize that affordable housing funding and programming are not just about building homes because many affordable housing developments include supportive services for residents that are much more difficult for these individuals to find elsewhere with fewer and fewer affordable units available in the face of increased need.

Case Study Abstract

The Federal Reserve Bank of San Francisco's Community Development Department and Housing California surveyed the state's affordable housing developers to learn how they are faring following the dissolution of redevelopment agencies (RDAs). California Gov. Jerry Brown proposed the dissolution of RDAs in 2011 as part of a larger measure to reduce the state's budget deficit, thereby taking away a tool that allowed cities and counties in California to recapture growth in property taxes as tax-increment financing for affordable housing and community infrastructure projects. The survey found the loss of RDAs came at a time that compounded an already difficult development environment following the recession.

Case Presentation

Note: The views expressed herein do not necessarily reflect the views of the Federal Reserve Bank of San Francisco or the Federal Reserve System.

INTRODUCTION

California's 400-plus redevelopment agencies (RDAs) played a critical role in the development of affordable housing across the state for over 60 years. Redevelopment agencies allowed cities and counties in California to recapture growth in property taxes as tax-increment financing for affordable housing and community infrastructure projects in order to improve conditions in designated areas that faced blight and disinvestment. Between 2001 and 2008 alone, 63,600 new affordable housing units were funded in part by RDAs—nearly half of them targeted to be affordable to those earning 50 percent or less of the area's median household income. In January 2011, California Gov. Jerry Brown proposed the dissolution of RDAs as part of a larger measure to reduce the state's budget deficit and cover general fund expenses, estimating that eliminating RDAs would recapture roughly \$1.7 billion per year in property tax revenues. Despite a prolonged policy effort to save or redesign RDAs in some form through legislation, the RDA program and its agencies were ultimately dissolved in 2012.

RDA dissolution was widely expected to have significant impacts on California affordable housing developers' ability to produce new projects. RDA funding allocations represented local government support of proposed housing developments and were often used to leverage more significant amounts of funding for a project through the federal Low Income Housing Tax Credit (LIHTC) Program. The majority of developments awarded 9 percent LIHTC credits in California in 2011 included RDA funds in their proposed development financing deals. Additionally, the redevelopment program was a longstanding and heavily-used source of funding for affordable housing in California, seen as a relatively stable and reliable resource as other affordable housing funding sources were frozen or cut during and after the 2007-2009 recession. In October 2015, over three years after the

unexpected loss of a significant funding source for affordable housing in California, the Federal Reserve Bank of San Francisco's Community Development Department and Housing California surveyed the state's affordable housing developers to learn how they are faring following RDA dissolution. The survey drew responses from 71 affordable housing development organizations across California. The respondents were equally distributed across the state geographically, and included regional nonprofit developers, for-profit developers, community development councils, and public housing authorities.

WANING RESOURCES AND DIFFICULTY LEVERAGING OTHER FUNDING WITHOUT RDA

In their responses, developers noted that the timing of the RDA loss is important, because it compounded an already difficult development environment following the recession. Without RDA funds to cover gaps in financing and without a replacement in sight for a depleted 2006 state housing bond program, developers are turning to other local sources of funding for gap costs, such as public housing authorities. Yet, these local agencies are also running low on financing dollars for new projects and contending with uncertainty around future funds. New construction projects are more difficult to fund without RDAs, respondents said, pushing developers to focus more on acquisition and rehabilitation projects. Some developers are also taking on smaller projects, which require less overall funding but result in lower developer fee returns and less cash flow.

To help fill the funding gap after RDA dissolution, some jurisdictions have created so-called "boomerang funds," local redevelopment-style tax-increment funding sources for affordable housing; 22 percent of respondents to our survey said they develop housing in these jurisdictions. At the state funding level, developers say they are looking into or planning to apply for funds through the new California Affordable Housing and Sustainable Communities Program and the Veterans Housing and Homelessness Prevention Program, among others. In response to our survey, 65 percent of developers said they have used or will be applying for new post-RDA sources of federal or

state funding in upcoming projects. Regardless of which new individual sources become available for affordable housing, though, respondents explain that none seem to be large enough to replace the amount of RDA funding previously available, and it is also unclear at this point how much funding these sources will provide over time.

LAND COSTS AND REGULATORY REQUIREMENTS SEEN AS SIGNIFICANT BARRIERS TO DEVELOPMENT

Eighty percent of respondents confirmed that RDA loss is significantly impacting site acquisition and remediation. In the past, the cost of acquisition was typically covered by public sources—often redevelopment funds. Respondents note that it is very difficult for them to outbid market-rate developers without RDA funds for site acquisition, so they are more likely to be diverted to less-desirable sites that are more affordable in land costs but end up adding costs in site readiness and remediation. Several respondents cited the difficulty of competing with market-rate developers not only for the prices they can pay but also their ability to close quickly on a land purchase and pay in cash, which affordable housing developers cannot do. Respondents pointed to the high cost of land around transit stations – light rail stations in particular – as a problem for affordable development, in part because transit proximity is highly valued in competitive affordable housing funding programs like LIHTC.

Respondents explained that a few jurisdictions are offering streamlined approval processes and fee waivers for affordable housing, but there is strong agreement among developers that new regulatory measures and programs at the state and federal level are too small to have significant impact in covering development costs. Furthermore, these new measures and programs do not go far enough to make up for the overall RDA loss, and often come with new compliance rules that can add to project costs. Several respondents stressed that the combination of increased regulation and fewer funding dollars is making it much more difficult to produce or rehabilitate affordable homes in California.

CHALLENGES IN ADAPTING BUSINESS MODELS AS RESOURCES FADE

After RDA dissolution and other funding cutbacks, some affordable housing developers are taking on more property management opportunities or other new lines of business, such as single-family development, consulting, and joint ventures with for-profit developers in order to stay in business. Others are taking their business out of California to states where land costs are lower and there are fewer regulatory hurdles. In some areas, public housing authorities have been designated as RDA successor agencies, which are responsible for managing the last RDA projects that were already in progress with dedicated funds before dissolution. Some respondents from these successor organizations note that they are being asked to do more work on more sites to cover these successor responsibilities without any added funding for staff and operations costs.

Moreover, over half of the respondents said that their organizations have had to cut staff due to reduced funding—some by as much as 30 to 50 percent of their total personnel. Many respondents observed that the past few years have been devastating to organizational stability and staff retention and development. Sixty-one percent of responding developers said they have had to reduce staff or make other organizational changes as a result of diminishing affordable housing funds.

AFFORDABLE FAMILY UNITS AT RISK

Our survey found that planned and future low-income family unit projects may be most at risk post-RDA. Sixty-two percent reported that they have had to adjust the unit mix of upcoming projects for funding reasons. Most developers said that they are increasingly focused on projects like special needs or veterans' housing because population-targeted program funding is among the only non-LIHTC funding available now. Several respondents said that they have had to convert proposed projects to predominantly market-rate units to make projects pencil out. Large family units are the most expensive to build, respondents explained, so they are much less likely to be

included in affordable housing developments now, despite an increased need for this type of supply in some markets.

Fully 90 percent of developer respondents reported that the need for affordable housing has increased in their markets in the past three years. One noted that “There are over 5,000 families on our waiting lists,” while another said, “We are opening a new 40-unit development in 2016 and we have over 450 people on an interest list for it.” They have seen the homeless population sharply grow in their markets. In areas where many residents work in the tourist economy and earn low wages, respondents said that the jobs-housing imbalance is very high, rental vacancies are few, and rent-controlled units are at risk when they turn over. With so many new funding programs focused on specific populations, developers say they are struggling to serve increased need among poor families.

AN EXPRESSED NEED FOR A PERMANENT SOURCE OF AFFORDABLE HOUSING FUNDS IN CALIFORNIA

Developers repeatedly emphasized that affordable housing funding and programming are not just about building homes. Many affordable housing developments include supportive services for residents that are much more difficult for these individuals to find elsewhere with fewer and fewer affordable units available in the face of increased need. The respondents see stable housing and services as closely intertwined and critical to stabilizing residents and lifting them out of poverty. As one respondent observed, “We need development dollars, but we also need resident service dollars. Low-income families and those with special needs need case management to help them stay housed. Developing one without the other is not addressing the root causes of poverty.”

Throughout their responses to our survey, developers repeatedly told us that they feel they now must accomplish more with fewer staff resources at a time of greater need for affordable homes in their markets. For these reasons, there is a resounding consensus among the responding developers that a permanent source of affordable housing funding in California is desperately needed to replace RDA funds, produce a much greater volume of needed affordable homes in communities across the state, and reduce uncertainty in the development process. ■

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California Tax Credit Allocation Committee

For a more thorough analysis of the survey and responses mentioned in this piece, see: Gabriella Chiarenza, “California Post-RDA Affordable Housing Developer Survey: Analysis of Results,” Federal Reserve Bank of San Francisco, 2015. <http://www.frbsf.org/community-development/publications/special/california-post-rda-affordable-housing-developer-survey/>

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Missing Middle Housing: Supplying Diverse Housing Options Along a Spectrum of Affordability

By **Dan Parolek, AIA**, OPTICOS DESIGN

KEY TAKEAWAYS

- Missing Middle Housing includes a range of vibrant building types found all over California: Duplexes, triplexes, fourplexes, courtyard apartments, bungalow courts, townhouses, live/work units, small multiplexes, and carriage houses, to name a few.
- The design range of this housing makes it available to a larger group of buyers or renters at a lower price point.
- This type of housing is defined by clear characteristics: Walkable context; medium densities and a perception that these building types are low density; small footprints and units; simple design; minimal off-street parking; embracement of community; and marketable appeal.
- Because of their simple forms and smaller size, Missing Middle building types can help developers maximize affordability and returns without compromising quality by providing housing types that are simple and affordable to build.

Case Study Abstract

“Missing Middle Housing” is a range of multi-unit or clustered housing types compatible in scale with single-family homes that help meet the growing demand for walkable urban living. This type of supply provides diverse housing options along a spectrum of affordability to support walkable communities, locally serving retail, and public transportation options. Furthermore, the design range of this housing makes it available to a larger group of buyers or renters at a lower price point. Missing Middle Housing provides a solution to the mismatch between the available U.S. housing stock and shifting demographics—combined with the growing demand for walkability.

Unfortunately, the solution is not as simple as adding more multi-family housing stock using the dated models/types of housing that we have been building. Rather, we need a complete paradigm shift in the way that we design, locate, regulate, and develop homes.

Case Presentation

The mismatch between current U.S. housing stock and shifting demographics, combined with the growing demand for walkable urban living, has been poignantly defined by recent research and publications by the likes of Christopher Nelson and Chris Leinberger, and most recently by the Urban Land Institute's publication, *What's Next: Real Estate in the New Economy*. Now is the time to stop talking about the problem and start generating immediate solutions.

Unfortunately, the solution is not as simple as adding more multi-family housing stock using the dated models/types of housing that we have been building. Rather, we need a complete paradigm shift in the way that we design, locate, regulate, and develop homes. As *What's Next* states, "It's time to rethink and evolve, reinvent and renew." A solution is "Missing Middle Housing," which is a varied range of supply that includes duplexes, fourplexes, bungalow courts, mansion apartments, and live-work units. These are a critical part of the solution and should be a part of every architect, planner, real estate agent, and developer's arsenal to encourage supply that meets consumer demand.

Well-designed, simple Missing Middle Housing types achieve medium-density yields and provide high-quality, marketable options between the scales of single-family homes and mid-rise flats for walkable urban living. They are designed to meet the specific needs of shifting demographics and the new market demand, and are a key component to a diverse neighborhood. They are classified as "missing" because very few of these housing types have been built since the early 1940s due to regulatory constraints, the shift to auto-dependent patterns of development, and the incentivization of single-family homeownership.

CHARACTERISTICS OF MISSING MIDDLE HOUSING

A WALKABLE CONTEXT

Probably the most important characteristic of these types of housing is that they need to be built within an existing or newly created walkable urban context.

Buyers or renters of these housing types are choosing to trade larger suburban housing for less space, no yard, and proximity to services and amenities, such as restaurants, bars, markets, and often work. Linda Pruitt of the Cottage Company, who is building creative bungalow courts in the Seattle area, says the first thing her potential customers ask is, "What can I walk to?" So this criterion becomes very important in her selection of lots and project areas, as is it for all Missing Middle Housing.

MEDIUM DENSITY BUT LOWER PERCEIVED DENSITIES

As a starting point, these building types typically range in density from 16 dwelling units per acre (du/acre) to up to 35 du/acre, depending on the building type and lot size. It is important not to get too caught up in the density numbers when thinking about these building types. Due to the small footprint of the building types and the fact that they are usually mixed with a variety of building types, even on an individual block, the perceived density is usually quite lower because they do not look like dense buildings.

A combination of these types gets a neighborhood to a minimum average of 16 du/acre. This is important because this is generally used as a threshold at which an environment becomes transit-supportive and main streets with neighborhood-serving, walkable retail and services become viable.

SMALL FOOTPRINT AND BLENDED DENSITIES

As stated, a common characteristic of these housing types are small to medium-sized building footprints. The largest of these types, the mansion apartment or side-by-side duplex, may have a typical main body width of about 40 to 50 feet, which is very comparable to a large estate home. This makes them ideal for urban infill, even in older neighborhoods that were originally developed for single-family lots but have been designated to evolve with slightly higher densities. As a good example, a courtyard housing project in the Westside Guadalupe Historic District of Santa Fe, New Mexico, sensitively incorporates six units and a shared community-room building onto a quarter-acre lot. In this project, the buildings are designed to be one room deep to maximize cross ventilation/passive cooling and to



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enable the multiple smaller structures to relate well to the existing single-family context.

SMALLER, WELL-DESIGNED UNITS

One of the most common mistakes by architects or builders new to the urban housing market is trying to force suburban unit types and sizes into urban contexts and housing types. The starting point for Missing Middle Housing needs to be smaller-unit sizes; however, the challenge is to create small spaces that are well-designed, comfortable, and usable. As an added benefit, smaller-unit sizes can help developers keep their costs down, thereby improving the pro-forma performance of a project, while keeping the housing available to a larger group of buyers or renters at a lower price point.

OFF-STREET PARKING DOES NOT DRIVE THE SITE PLAN

The other non-starter for Missing Middle Housing is trying to provide too much parking on site. This ties back directly to the fact that these units are being built in a walkable urban context. The buildings become very inefficient from a development potential or yield standpoint and shifts neighborhoods below the 16 du/acre density threshold, as discussed above, if large parking areas are provided or required. As a starting point, these units should provide no more than one off-street parking space per unit. A good example of this is newly constructed mansion apartments in the new East Beach neighborhood in Norfolk, Va. To ensure these lower off-street parking requirements work, on-street parking must be available adjacent to the units. Housing design that forces too much parking on a

site also compromises the occupant's experience of entering the building or "coming home" and the relationship with its context, especially in an infill condition, which can greatly impact marketability.

SIMPLE CONSTRUCTION

The days of easily financing and building complicated, expensive Type I or II buildings with podium parking are behind us, and an alternative for providing walkable urban housing with more of a simple, cost-effective construction type is necessary in many locations. The *What's Next* publication states, "Affordability – always a key element in housing markets – is taking on a whole new meaning as developers reach for ways to make attractive homes within the means of financially constrained buyers." Because of their simple forms, smaller size, and Type V construction, Missing Middle building types can help developers maximize affordability and returns without compromising quality by providing housing types that are simple and affordable to build.

CREATING COMMUNITY

Missing Middle Housing creates community through the integration of shared community spaces within the types, as is the case for courtyard housing or bungalow courts, or simply from the proximity they provide to the community within a building and/or the neighborhood. This is an important aspect of this housing particularly due to the growing market of single-person households (which is nearly 30 percent of all households) that want to be part of a community. This has been especially true for single women who have proven to be a strong market for

these Missing Middle Housing types, especially bungalow courts and courtyard housing.

MARKETABILITY

The final and maybe the most important characteristic in terms of market viability is that these housing types are very close in scale and provide a similar user experience (such as entering from a front porch facing the street versus walking down a long, dark corridor to get to your unit) to single-family homes. Thus, there is a less drastic mental shift for potential buyers and renters than if they were to live in a large mid-rise or high-rise project. This, combined with the fact that many baby boomers likely grew up in similar housing types in urban areas or had relatives who did, enables them to easily relate to these housing types.

This is a call for architects, planners, and developers to think outside the box and to begin to create immediate, viable solutions to address the mismatch between the housing stock and what the market is demanding—vibrant, diverse, sustainable, affordable, and walkable urban places. Missing Middle Housing types are an important part of this solution and should be integrated into comprehensive and regional planning, zoning code updates, transit-oriented development strategies, and the business models of developers and builders who want to be at the forefront of this paradigm shift.

The market is waiting. ■

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He is also at the forefront of rethinking the way we zone our communities to promote more compact, walkable, and vibrant places. In 2007, he co-authored the book *Form-Based Codes* and, in 2013, as part of a larger sustainable growth strategy in partnership with the Prince's Foundation for Building Community, he wrote the first development code for Gabon, Africa. He serves as a board member for the Form-Based Codes Institute, an organization dedicated to reforming zoning to remove barriers for urban development, and for TransForm, which promotes walkable communities with transportation choices to connect people of all incomes to opportunity. His love of good urbanism springs from a childhood spent exploring the vibrant downtown of Columbus, Nebraska, on his bike.

Los Angeles at a Crossroads: The House LA Initiative

By **Councilmember Gil Cedillo**, 1ST DISTRICT COUNCIL, CITY OF LOS ANGELES

KEY TAKEAWAYS

- A revision of the Housing Element of Los Angeles' General Plan (2006-2014) shows that only 50,000 housing units were built, fulfilling less than 50 percent of the City's Regional Housing Needs Assessment (RHNA) goal of 112,876 units for the previous Housing Element period.
- Due to crushing budget cuts and the dissolution of the Community Redevelopment Agency, the Housing and Community Investment Department of Los Angeles (HCIDLA) can only commit to financing approximately 500 units per year in the new Housing Element (2014-2021). This gravely affects the city's ability to meet its housing challenges.
- The House LA Initiative aims to cut red tape and streamline building in Los Angeles, while offering bureaucratic relief in order to facilitate smart growth and maintain and increase affordability. In the absence of funding to create the housing the city needs, the greatest asset a municipality owns is land use.

Case Study Abstract

Los Angeles has fared poorly in planning for future population growth, but the House LA Initiative seeks to address the city's severe housing shortage via steps taken at the local level to solve a lack of supply, including affordable housing. The 2014-2021 Regional Housing Need Allocation Plan (RHNA) from the Southern California Association of Governments determines a need for 82,002 housing units in the city of Los Angeles. The House LA Initiative would expedite the Environmental Impact Review (EIR) process, as well as re-examine the city's site plan review approval process as a strategy to increase the city's affordable housing production. Other measures include encouraging the production of micro-units and facilitating accessory dwelling units.

Case Presentation

Los Angeles is currently at a crossroads and it is up to all of us to decide what type of Los Angeles we want to plan for. In recent years, we have set the course for a progressive Los Angeles that focuses not only on core services but also creating sustainability with multi-modal transportation plans as well as increasing the minimum wage. Yet, one issue Los Angeles has fared poorly on has been planning for future population growth.

A revision of the Housing Element of Los Angeles' General Plan (2006-2014) shows that only 50,000 housing units were built, fulfilling less than 50 percent of the City's Regional Housing Needs Assessment (RHNA) goal of 112,876 units for the previous Housing Element period.

Supply-side economics dictate that when demand exceeds supply, prices will rise. This rise has led to conditions where rents continue to increase to the point where low-income individuals are living in overcrowded, unpermitted housing. They are also commuting long distances to avoid high housing costs in the urban core, and in the process are increasing regional traffic. This supply-demand dilemma has priced people out of the major metropolitan areas.

Los Angeles, for example, remains the nation's most unaffordable housing market. While rent is considered affordable when it consumes no more than 30 percent of household income, the average renter in Los Angeles pays nearly 47 percent of his income toward rent. Over 75 percent of the lowest-income households pay half of their incomes or more toward rent, rendering them severely rent burdened. The lack of affordable housing may in part be due to the decrease in local and state funding.

From 2006-2014, on average, the Housing and Community Investment Department of Los Angeles (HCIDLA) financed 1,200 affordable housing units per year, at the peak of the Community Redevelopment Agency's (CRA) golden years. Due to crushing budget cuts and the CRA's dissolution, the HCIDLA can only commit to financing approximately 500 units per year in the new Housing

Element (2014-2021). This gravely affects the city's ability to meet its housing challenges.

In addition, the gap between owners and renters in Los Angeles continues to grow. According to the 2016 Renter Survey from the CALIFORNIA ASSOCIATION OF REALTORS®, homeownership remains important to renters, with nearly half (45 percent) rating it 8 or higher in importance on a scale of 1-10, with 10 being extremely important. Nearly half of renters (48 percent) plan to buy a home in the future. First-time home buyer programs are essential in reaching the American dream and creating communities.

In 2011, the city funded over 500 homeownership loans for first-time buyers citywide. It offers a modest silent second, which allocates up to \$60,000 per family for buyers who have not had an ownership interest in any real property at any time during the last three years, and plan to occupy the residence. But in today's market, that offers little hope for down payment or closing cost relief, so we have to do more.

To this point, I have introduced legislation asking for a comprehensive analysis of our current first-time home buyer program, with the hope that we can increase the down payment assistance amount and expand participation by raising the income requirements. This will make a small dent in the larger scheme of things of turning renters into homeowners, but the issue of having enough housing stock is the elephant in the room.

Looking into the future, the Southern California Association of Governments' (SCAG) 2014-2021 Regional Housing Need Allocation Plan (RHNA) determines a need for 82,002 housing units in the city of Los Angeles. This means a production rate of approximately 10,250 units per year (5,823 affordable units per year). In order to meet this goal, along with past years of low production, we must invest in reforms that work.

As the Chair of Housing for the city of Los Angeles, I introduced the House LA Initiative. I hope to cut red tape and streamline building in Los Angeles, while offering bureaucratic relief in order to facilitate smart growth and maintain and increase

affordability. In the absence of funding to create the housing we need, we must use the greatest asset a municipality owns, land use.

The House LA Initiative continues to grow and has sought out-of-the box solutions to ease the burden. Within our own Planning Department, we seek to expedite the Environmental Impact Review (EIR) process, which could save 30 to 50 percent of time for projects. With site plan review modifications, we seek to amend the site plan review ordinance, including the option to increase the threshold from 50 residential units to a higher amount, and re-examine the approval process as a strategy to increase the city's affordable housing production. Because density is a challenge, our micro-unit motion evaluates the Greater Downtown Housing Incentive Ordinance as a model to encourage the production of micro-units, as well as the potential impact micro-units can have on our affordable housing needs and the benefit of expanding this model to apply to other geographic areas of the city.

House LA also seeks to expand the city's shared vehicle program by permitting the substitution of one shared vehicle for every four required parking spaces for residential or mixed-use buildings located in or within one-fourth a mile of a transit corridor.

I also want to identify options for preserving unapproved second housing units, and creating a permit process to allow the development of accessory dwelling units in accordance with Assembly Bill 1866, which encourages accessory dwelling units by requiring cities to reduce or eliminate local barriers to their development. Last but certainly not least, we seek to use city-owned land as sites for affordable housing developments.

These are short-term fixes to help increase our housing stock. The larger discussion has been around financing the 10,000 a year production goal. Lastly, we continue to advocate for additional revenue sources.

For months, the Los Angeles City Council has undertaken a serious discussion about funding the housing crisis. The City Attorney prepared two ballot options to place before voters for the November 2016 general election. Both options include supportive housing, homeless facilities, and affordable housing. The county and the state are also putting forth their own funding strategies to address the housing crisis.

Our housing challenges were not created overnight, nor will they be fixed overnight. There are short-term solutions that we are prepared to undertake, which are well within the realm of our jurisdiction. The county of Los Angeles and the state of California have joined in the conversation, and are acting on parallel tracks to finance the production of housing and strengthen housing programs. Our crisis affects our homeless populations, those who are being priced out of the rental market, and those who seek to become homeowners. The city's solution should be inclusive of all these challenges and be comprehensive. The future of Los Angeles is in our hands. ■

Councilmember Gil Cedillo was elected to the Los Angeles Council, First District, in May 2013. He brings 14 years of legislative experience to the City Council after having served in the California State Assembly and the State Senate. During his terms in the state legislature, Councilmember Cedillo authored over a hundred bills that were signed into California law by four different Governors that include Pete Wilson, Gray Davis, Arnold Schwarzenegger, and Jerry Brown.

Councilmember Cedillo chairs the city's Housing Committee, where he continues to advocate for equity for all residents. Cedillo promotes an increase in our housing stock and believes in smart growth to help revitalize our neighborhoods and to create jobs. Cedillo consistently endorses and champions Los Angeles as a leading global city.

Cedillo grew up in the Boyle Heights area of Los Angeles and attended Roosevelt High School. Cedillo graduated from the University of California Los Angeles with a Bachelor's Degree in Sociology in 1977 and received a Juris Doctor degree from the Peoples College of Law in 1983.

Preserving Existing Affordability Through a Social Purpose REIT

By **Drew Ades**, HOUSING PARTNERSHIP EQUITY TRUST

KEY TAKEAWAYS

- The Housing Partnership Equity Trust (HPET) is a social purpose real estate investment trust (REIT) that provides a private market, mission-driven solution for preserving affordable housing across the country.
- HPET is designed to be a quick, flexible, and reliable investment platform so that it may compete directly with for-profit, market-rate buyers. Once the Housing Partnership Equity Trust has acquired a property, it ensures rents are set at levels affordable to target residents.
- To date, HPET has raised \$85 million in equity and has used it to purchase 10 properties, in five states, totaling 2,540 homes.

Case Study Abstract

New tools are needed to ensure safe and affordable housing is available for all income levels as the nation's rental affordability crisis affects individuals and families across the income spectrum. Naturally occurring affordable housing either falls out of the marketplace after severe disinvestment and deterioration, or moves out to the top of the market through increased rent or conversion to ownership, and this disappearing stock is prohibitively expensive to replace. A social purpose real estate investment trust (REIT), such as the Housing Partnership Equity Trust (HPET), provides a private market, mission-driven solution for preserving affordable housing across the country. The trust's unique structure allows for long term ownership and preservation of affordability at HPET-owned properties.



Savannah at Southport Apartments in West Sacramento, California. HPET purchased this 228-unit mixed-income property with Eden Housing in March 2016.

Case Presentation

RENTAL CRISIS

Rental affordability is now a national crisis. In 2013, just under half of all renters nationwide were cost burdened—defined as paying more than 30 percent of their income in rent. This burden is greatest among minority households and in high-cost coastal markets such as Los Angeles. According to the National Low Income Housing Coalition, the 2016 mean hourly wage for renters in California is \$19.22 per hour, while the wage required to afford a two-bedroom apartment in California is estimated at \$28.59 per hour. This rental burden is no longer limited to low-income families but increasingly affects individuals and families across the income spectrum. As the pressures on the rental market increase and development of new units fails to keep pace, new tools are needed to ensure safe and affordable housing is available for all income levels.

Rental housing supported by federal programs, such as the Department of Housing and Urban Development's (HUD) public housing and Section 8 and the Low Income Housing Tax Credit, currently account for less than 15 percent of the total rental stock in the United States. At the low end of the income spectrum, we only serve about 25 percent of the families who are income eligible for federal rental assistance through these programs. With continued budget austerity in Washington, the significant increase to these resources that is required to meet the current need is unimaginable, and we must look elsewhere for solutions. In fact, most low-income renters already live in the unsubsidized rental market, which makes up the majority of rental housing in the United States.

The supply of safe, affordable rental housing is becoming increasingly scarce as the existing, naturally occurring affordable housing either falls out of the marketplace after severe disinvestment and deterioration, or moves out to the top of the market through increased rent or conversion to ownership. According to Harvard's Joint Center for Housing Studies, more than 2 million units are at risk of being lost over the next decade. This disappearing stock is prohibitively expensive to replace. As families are forced to pay a larger percentage of their income in

rent, they sacrifice spending on other necessities like health care and food. The increase in housing cost burden will also likely lead to other negative consequences for society, as research increasingly shows that stable housing is linked to health, education, and job success for families.

HOUSING PARTNERSHIP EQUITY TRUST: AN OVERVIEW

The Housing Partnership Equity Trust (HPET) is a social purpose real estate investment trust (REIT) that provides a private market, mission-driven solution for preserving affordable housing across the country. HPET uses a new "impact investment" approach to attract values-based private capital to address the growing rental affordability crisis. HPET is structured as a REIT, which is an investment vehicle, sometimes referred to as a mutual fund for real estate, that enables smaller-scale investors to invest in a company which owns or finances income-producing real estate.

HPET was started by the Housing Partnership Network (HPN), a national business collaborative of high-performing affordable housing and community development nonprofits, and 12 nonprofit partners as a vehicle to attract new sources of capital to combat the growing affordable housing crisis. HPET uses its capital to partner with its nonprofit members to acquire and preserve multi-family properties serving low and moderate-income renters. The original 12 nonprofit partners are among the nation's preeminent affordable housing developers and operators, including four organizations in California: Bridge Housing, Eden Housing, LINC Housing Corporation, and Mercy Housing. In addition to contributions from HPN and the partners, initial seed capital was provided by Prudential Insurance Company, the John D. and Catherine T. MacArthur Foundation, and the Ford Foundation. Subsequent investors include Citi, Morgan Stanley, and Charles Schwab Bank.

HOW IT WORKS

HPET is designed to be a quick, flexible, and reliable investment platform so that it may compete directly with for-profit, market-rate buyers. Once the Housing Partnership Equity Trust has acquired a

property, it ensures rents are set at levels affordable to target residents – typically families earning between 50 to 80 percent of area median income – and experienced, mission-driven management focuses on the needs of the residences. The unique structure allows for long term ownership and preservation of affordability at HPET-owned properties.

In collaboration with the partners, HPET acquires affordable rental properties located in so-called “opportunity areas” near jobs, schools, transportation, and other community amenities. We believe the location of the homes we own is crucial to fulfilling our mission of improving the lives of our residents and communities. This belief is supported by recent research that shows when young children from poor families grow up in opportunity neighborhoods, they have a much better chance of escaping poverty, as demonstrated through increased lifetime earnings and higher college attendance rates.

Active asset management by the partners allows HPET to maintain the affordability of these properties and achieve consistent cash flows and reliable returns for investors. HPET is committed to providing three types of return: Economic return from the assets, social return through preserving affordable housing, and environmental return through energy efficiencies at HPET-owned properties.

All HPET properties are purchased in a joint venture with one of our non-profit partners, who are also HPET investors. This collaboration allows the REIT to leverage the partners’ market knowledge and existing infrastructure to ensure the best outcomes

for the residents and our investors. After making its first investment in April 2013, HPET declared its initial dividends on both its common and preferred stock in the third quarter of 2015.

To date, HPET has raised \$85 million in equity and has used it to purchase 10 properties, in 5 states, totaling 2,540 homes. HPET owns two properties in California with Eden Housing, Savannah at Southport in West Sacramento, and Woodside Court Apartments in Fairfield. ■

For more information about the Housing Partnership Equity Trust, contact Drew Ades, President and CEO, Housing Partnership Equity Trust at ades@hpequitytrust.org or go to www.hpequitytrust.com.

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Drew Ades is President and CEO of the Housing Partnership Equity Trust. He joined in November 2011 as the founding President and CEO of the social venture Real Estate Investment Trust (REIT). He previously served as Director of Multi-family Risk for Fannie Mae and Co-President of CAM LLC, a wholly owned subsidiary real estate operating company created to preserve and enhance the affordability and sustainability of multi-family properties owned by Fannie Mae. As Director of Multi-family Risk, Ades was the driving force behind the creation of Fannie Mae’s Multi-family Green Initiative, overseeing the launch of “Green Refi Plus,” a loan product developed in partnership with the Federal Housing Authority within the U.S. Department of Housing and Urban Development to finance the “green” renovation of affordable rental properties.

Ades was also responsible for Fannie Mae’s partnership with the U.S. Environmental Protection Agency to create an “Energy Star” rating for multi-family properties, and served as the credit officer for the Multi-family Pool channel, responsible for the acquisition, closing, and special asset management of more than \$25 billion in multi-family loans. Prior to joining Fannie Mae, he was Washington Chief of Staff for U.S. Rep. Robert E. Andrews, and previously served as Treasurer and Vice Chair of the Washington D.C.-based nonprofit Greenhome/GreenSpace.