

INFORMATIONAL HEARING SENATE TRANSPORTATION AND HOUSING COMMITTEE

Tuesday, March 7, 2017
1:30 p.m. — John L. Burton Hearing Room (4203)

California's Housing Crisis: Long-Term & Comprehensive Funding and Regulatory Solutions

Background Information

Purpose of the Hearing

The purpose of this Senate Transportation and Housing Committee hearing is to:

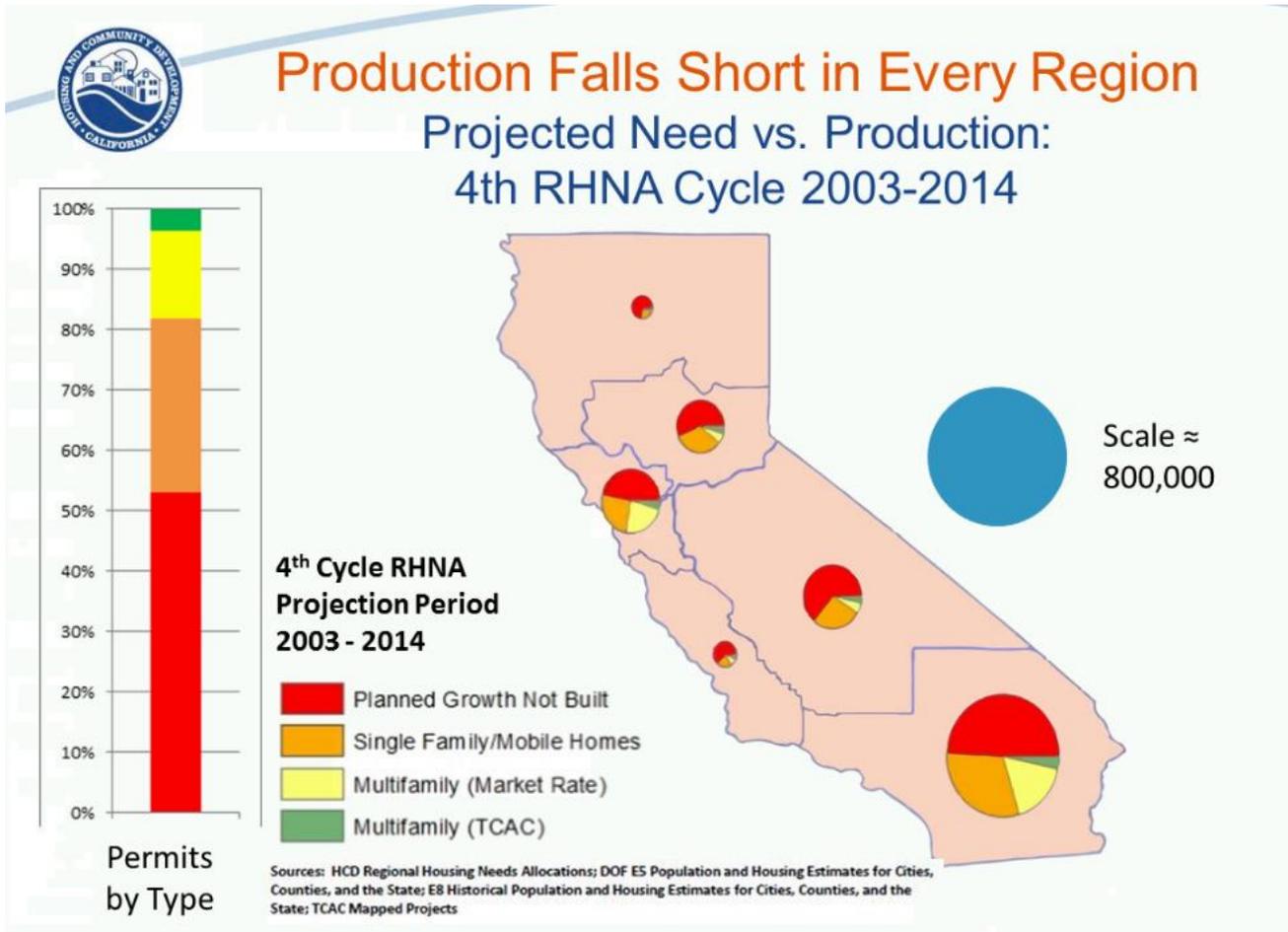
- 1) Discuss the need for more housing across income levels
- 2) Identify critical existing state and federal programs, and understand potential changes and cuts at the federal level under President Trump and a Republican-controlled congress
- 3) Understand what factors contribute to California's high housing prices and rental costs
- 4) Discuss what California can do to increase access to and encourage the construction of affordable housing following the loss of redevelopment funds and the exhaustion of voter-approved bond funds and without a permanent source of funding
- 5) Discuss what California can do to encourage homeownership, particularly for first-time homebuyers.

This background paper will provide an overview of the cost of housing for low-income earners and the cost of single-family homes, particularly the impact on first-time homebuyers. This background paper will also discuss land use policies and public opposition to higher-density development that disincentivize the construction of housing.

Overview

California's home prices and rents are higher than just about anywhere else in the country. This has dramatic impacts not only for California households across all income levels, but for the state's overall economy. According to a recent report from the California Department of Housing and Community Development (HCD), over the last 10 years, California has built an average of 80,000 homes a year, far below the 180,000 homes needed each year to keep up with housing growth from 2015-2025. This is not a new phenomenon; California has failed to add sufficient housing to keep pace with population growth since the 1970s. Another recent report published by the McKinsey Global Institute concludes that to satisfy existing needs, California must build 3.5 million homes by 2025. The McKinsey report further estimates that in dollar terms, California loses \$140 billion per year in output or 6% of state gross domestic product due to the housing shortage (\$90 billion in missing construction investment and more than \$50 billion per year in

missing consumption that is crowded out by housing costs). HCDs estimates are more extreme. It finds that the housing costs to the economy are \$238 billion annually.

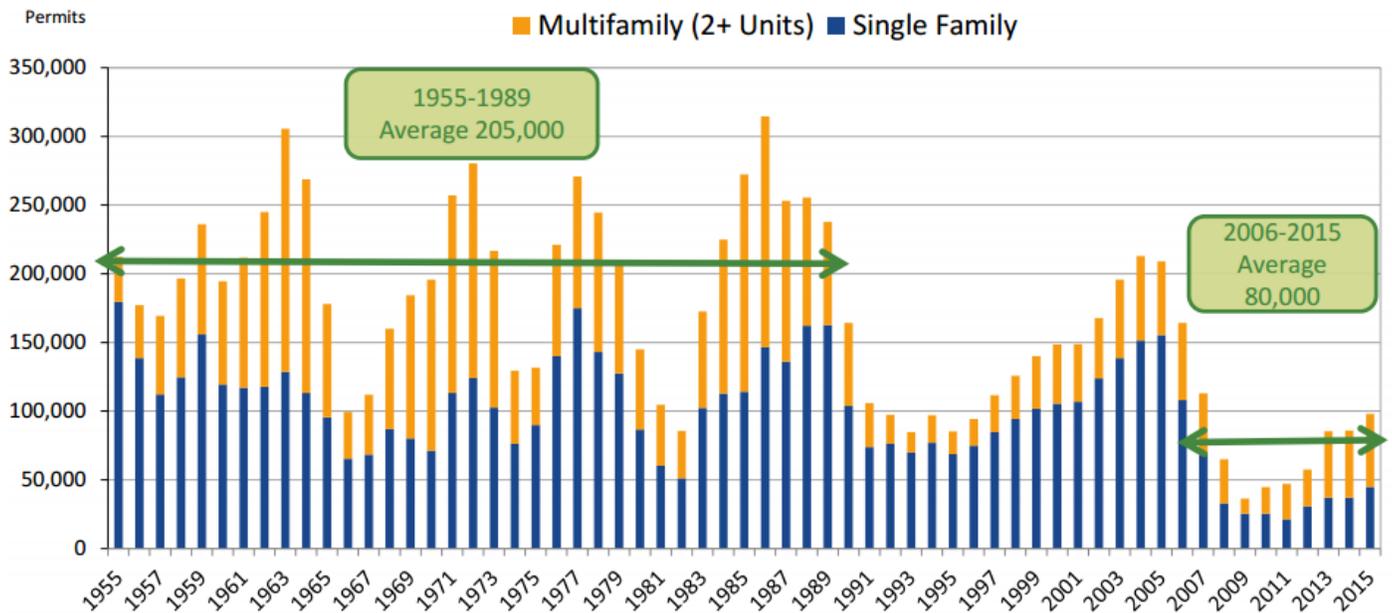


Note: In the chart above, the production rate for housing affordable to those below 60% of the area median income is below 5% of the total permits and the rate for multifamily housing is around 15%.



Annual New Housing Permits Statewide 1955-2015

Annual Production of Housing Units 1955-2015



Source: Construction Industry Research Board/California Homebuilding Foundation Reports 2005, 2013, 2015; Graphic by HCD

Why does California continually under produce housing, and what can we do about it? Three fundamental structural problems severely constrain the ability of California to meet its housing needs:

- 1) Many families are simply not able to pay market rates for adequate housing, and public investment is insufficient to cover this gap.
- 2) Many local governments believe that housing does not pay for itself under the current tax structure, making them hesitant to embrace new residential development.
- 3) The land use permitting and approval process responds to public antipathy to development generally, to high-density development more specifically, and to rental housing and affordable housing in particular.

Housing Prices

This section will explore some of the trends in the rental and homeownership market in California.

Rental Market

California has become one of the most expensive places to live in the country, which has had a dramatic impact on the middle class and the working poor. Low-income housing units, if available, are often in serious states of disrepair, and working families are unable to make rent payments on their “affordable” housing rents. Additionally, California requires the third-highest wage in the country to afford housing, behind Hawaii and Washington, D.C. In California, the

average asking rent is \$1,889. To afford this level of rent and utilities without experiencing high-cost burden — in other words, with paying more than 30% of income on housing — a household must earn an hourly “housing wage” of \$36.33 per hour. This means that a person must earn 3.6 times the minimum wage to afford average asking rental prices.

Furthermore, California’s 2.2 million extremely low-income (ELI) and very low-income (VLI) renter households are competing for only 664,000 affordable rental homes. This leaves more than 1.54 million of California’s lowest income households without access to affordable housing in a state with 21 of the 30 most expensive rental housing markets in the country. VLI households are those that earn less than 50% of the area median income, while ELI households earn less than 30%.

As a result, low-income families are forced to spend more and more of their income on rent, which leaves little else for other basic necessities such as transportation, food, health expenses, child care, and other needs. It also means that many renters must postpone or forego homeownership, live in more crowded housing, commute further to work, or, in some cases, choose to live and work elsewhere.

Households in MSA unable to afford rent

Thousand



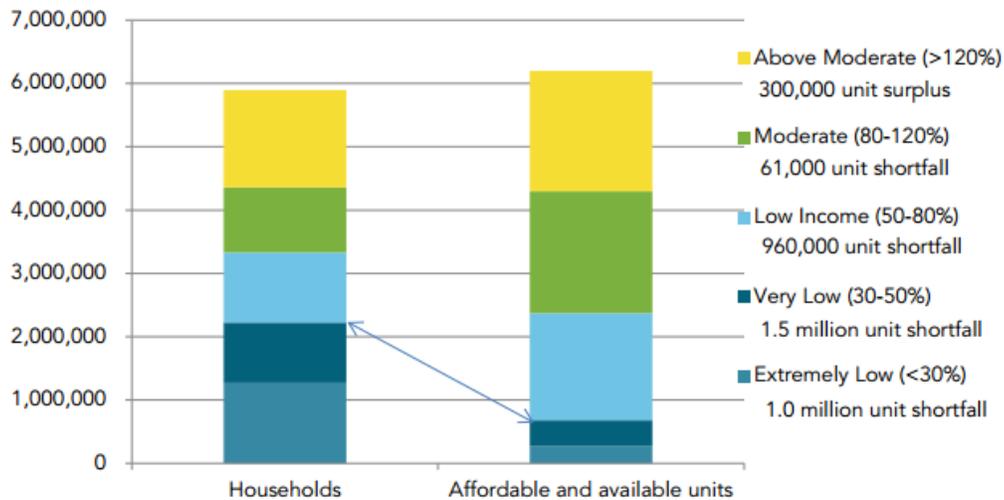
The chart to the left shows numerically how many households by the thousands in each metropolitan statistical area are unable to afford rent. The red color chart signifies the share of households unable to afford rent out of the total households in the metropolitan statistical area. Note that the shaded areas represent 98% of the state population. The unshaded areas represent 2%.

High-cost burden and severe housing-cost burden (paying more than 50% of income towards housing) are rapidly spreading among moderate-income households. In the 10 metropolitan areas with the highest median-housing costs nationwide, 75% of renter households earning \$30,000 - \$44,999 and 50% of those earning \$45,000 - \$74,999 were experiencing housing cost burden in 2014.

SOURCE: US Census Bureau; Zillow; McKinsey Global Institute analysis

Rental Housing Falls Short at All Income Levels, Except Above Moderate

Comparison of Households and Affordable and Available Units in California



Source: 2016 National Low Income Housing Coalition tabulations of 2014 American Community Survey Public Use Microdata Sample (PUMS) housing file. Graphic by HCD.

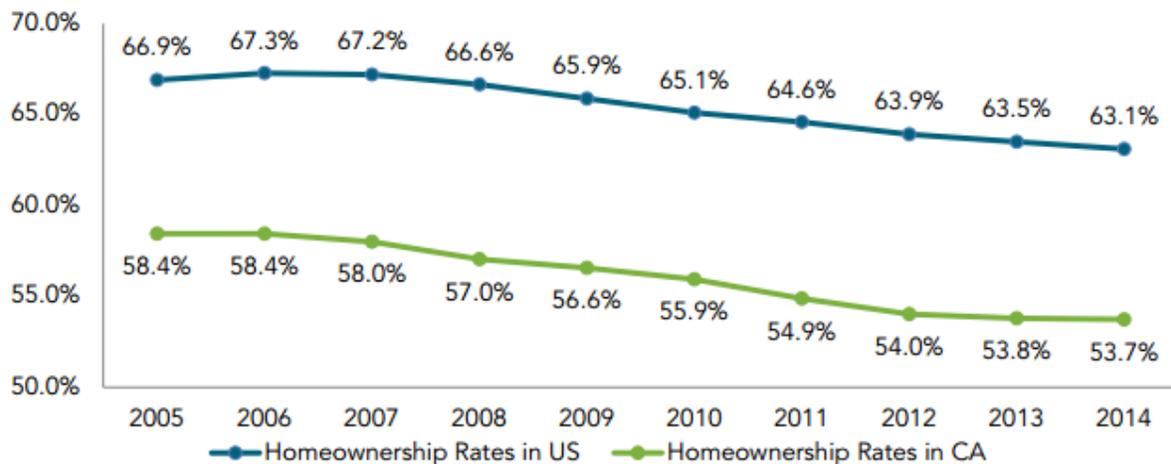
Homeownership

According to the HCD, since the 1950s, California's homeownership rate has fallen below the national rate, with a significant gap persisting since the 1970s. More recently, between 2006 and 2014, the number of units that were owner-occupied fell by almost 250,000 in California, while the number of rental units increased by almost 850,000. California's homeownership rates have fallen to 53.7%, the lowest rate since the 1940s. Compared to other states, California has the third lowest homeownership rate.

California's home prices have also risen faster than in the rest of the country due to years of low housing production. The highest home prices can be found along the coast, with the average median in San Francisco in August 2016 at more than \$1.25 million; the statewide median single-family home price was \$526,580. The California Association of Realtors estimates that only 34% of households in California can afford to purchase the median home in the State.

Potential homebuyers aged 30 and under face the biggest challenge in buying a home in the current market. According to the California Association of Realtors (CAR) Annual Housing Market Survey, this group of young consumers not only has a lower household income than other age groups, but they also make a smaller down-payment when purchasing a property. This means they are in the age group that is the least qualified to buy a median-priced home. Many of them tend to purchase their home in the lower-priced segment, which is also the most competitive market with the tightest housing supply. Not surprisingly, this is also the age group with the most first-time buyers.

Recent Homeownership Rates Nationally and in CA 2005-2014



Source: U.S. Census Bureau, 2005-2009, 2011-2014 American Community Survey 1-Year Estimates, B25003, 2010 Decennial Census, General Housing Characteristics, QT-H1. Graphic by HCD.

First-time homebuyers are among the hardest hit by rising home prices and rising interest rates. According to CAR, in 2016, the share of California first-time homebuyers was 29.2%, a decline from the 50.8% peak of first-time homebuyer market share in 1995. The rate was slightly lower than the 2015 rate of 29.5%, remained below the long-run average of 38%, and was the second lowest in the last ten years. A number of factors contributed to the decrease of homeownership, including student debt, affordability, lack of interest, and convenience of living with parents.

The low level of first-time homebuyers and high housing prices are concerning because it signals a constrained flow of new households into the housing market. Fewer first-time homebuyers also slow down the housing recovery process. This means that more potential homeowners are continuing to rent, which creates greater competition for a limited number of rental units. Without a steady stream of new households into homeownership, the trade-up market cannot be replenished in the long run.

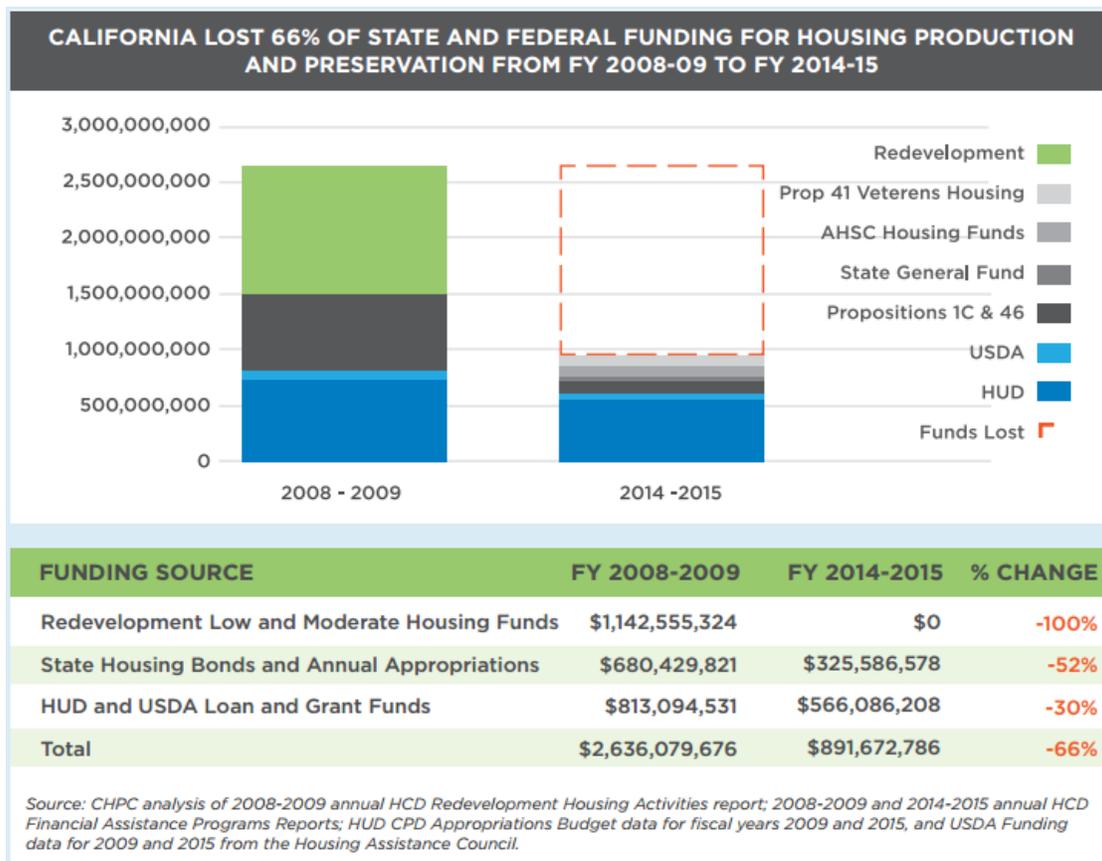
Housing Funding

Economic and social policies continue to contribute to the lack of housing in California and are particularly relevant as President Trump assumes office. While changes at the federal level are uncertain, President Trump committed on the campaign trail to increase defense spending at the expense of non-defense spending, which could mean billions of dollars in cuts to housing and other anti-poverty programs. In addition, President Trump has said he wants to cut non-defense spending by 1% every year, which would be devastating to affordable housing programs including Housing Choice (Section 8) vouchers, public housing, and project-based rental assistance.

California has also seen a significant reduction of funding at the state level in recent years. Proposition 46 of 2002 provided \$2.1 billion for a variety of affordable housing programs, and Proposition 1C of 2006 provided an additional \$2.85 billion. As important as housing bonds are, they are a short-term strategy. Both Prop 46 and Prop 1C provided roughly 4-5 years of funding, and the state's Department of Housing and Community Development has awarded just about all of these funds. California also recently lost tax increment as a funding stream for affordable housing with the dissolution of redevelopment agencies. With the loss of redevelopment and

expenditure of the last voter-approved housing bonds, \$1.5 billion of annual state investment dedicated to housing has been eliminated.

The State has made efforts to fill these funding gaps through the passage of \$2 billion in bonds to establish the “No Place Like Home” program, \$150 million in new funding for homeless programs in the 2016 Budget Act, \$600 million for the Veterans Housing and Homelessness Prevention Program in 2014, and 20% allocation of the Greenhouse Gas Reduction Fund revenues to fund the Affordable Housing Sustainable Communities Program, with at least half of those funds for affordable housing. Additionally, in November 2016, several local jurisdictions approved \$2.7 billion in local bonds, along with two local sales tax increases for affordable housing. The figure below, however, demonstrates that these funds are not sufficient to fill the existing funding gap.



Land Use Policies

The concept of the “fiscalization of land use” is familiar to many. The problem, however, is not that land use decisions are “fiscalized” but that the incentives all favor outcomes that are biased against housing development. Ever since the passage of Proposition 13 in 1978, property taxes have constituted a diminishing source of revenue for governments. This situation was exacerbated in the early 1990s when the tapped local property tax revenues to meet its obligation to the public schools through the Education Revenue Augmentation Fund (ERAF). In many cases, the additional revenues a local government now earns from each new housing unit are insufficient to cover the added expense of providing services to the new residents of that home. Some of the fixed costs of infrastructure can be recouped through fees (which, of course, reduce the affordability of the home), but the on-going service costs remain at issue. Thus, a city council

deciding the fate of a new housing development faces the unenviable dilemma of denying needed housing or reducing services to existing constituents. As one might expect, the choice often is made in favor of the existing constituents.

At the same time, when a city council considers an alternate proposal to develop a parcel of land as a retail center, the fiscal incentives strongly support approval. Local governments receive a large portion of all sales tax revenue generated within their borders. The additional revenue received from a large retail facility, such as a big-box retailer or a car dealer, easily outweighs the costs of providing services to the facility. Local government can use these surplus revenues to enhance services to its constituents. As a result, housing is subject to a double whammy. Not only can it be difficult to get approval for a new housing development on residentially-zoned land, but more land is zoned commercial in the hope that retail establishments can be attracted. The only real fiscal incentive local governments have to approve housing is so that there are enough residents to support the retailers.

Addressing public opposition to higher-density development

Political pundits have noted that the only thing the public seems to dislike more than sprawl is high density development. Moreover, there remains in many communities a stigma against rental housing generally and affordable housing in particular. Though largely debunked by evidence and experience, fears of blight, increased crime, and decreased property values fuel these biases. These views manifest themselves in the political arena when communities create their zoning ordinances and when multi-family housing developments are forced to go through the local land use permitting and approval process. Bowing to political pressure, local planning commissioners and elected officials often seek to limit residential zoning densities and to deny or significantly scale back proposals for affordable housing developments. In the meantime, California's population continues to grow and housing prices spiral out of reach of an ever larger number of households.

To provide safe and decent housing for all Californians, we must ensure that the local land use process balances the views of the community with the larger regional and statewide housing need. Current housing element law requires local governments to plan for their fair share of the region's housing needs. Under state law, a housing element must identify adequate sites that are appropriately zoned to facilitate the development of housing affordable to all income segments of the community.

One limitation of housing element law is that it lacks teeth. While the large majority of cities and counties in the state have adopted adequate housing elements, a significant percentage of the state's local jurisdictions have failed to comply with the law. Enforcement depends on private developers or non-profit lawyers suing cities and counties that are in non-compliance. In instances where the court does find cities or counties out of compliance, remedies are limited. The court may order the jurisdiction to adopt an adequate housing element and may halt development in the community in the meantime. For local governments that do not have major commercial or industrial projects pending, this is equivalent to no remedy at all. Ultimately, there must be stronger consequences for local governments that fail to comply with the law.

A second limitation of housing element law is that it requires only planning, not production. A city or county that zones enough land at the correct densities to accommodate its housing needs has complied with the law, regardless of whether any units are ever built on these sites. Because

local governments do not control housing production, it is unfair to hold them accountable for production. Therefore, encouraging production must be done with incentives.

Conclusion

High housing costs and shortage of housing stock in California directly affect the future health of California's economy. As the economy continues to rebound, however, both the federal and state governments must give serious consideration to funding programs that encourage the construction of and access to housing that is affordable to all income levels. Additionally, as home values continue to rise, this is an opportune time to identify the economic realities facing potential homeowners and evaluate existing programs that assist first-time homebuyers. Policy makers must also consider what barriers local governments face in keeping up with housing demands.

Biographies

Matt Schwartz, President & CEO — California Housing Partnership Corporation. Mr. Schwartz plays a leadership role in in shaping state and federal housing-related legislation and regulations to expand the resources to preserve and create affordable housing for the state's lowest income residents. Mr. Schwartz has worked in the development, planning and financing of affordable housing for 25 years in both the private and public sectors. Mr. Schwartz was appointed to the San Francisco Housing Authority Commission by Mayors Newsom and Lee, is a past President of the Board of Housing California, a member of the Board of the NonProfit Housing Association and an active participant in the National Affordable Housing Preservation Working Group. Mr. Schwartz received a Master's Degree in Public Policy from Harvard's Kennedy School of Government and a Bachelor's Degree from Stanford University. He is a recipient of the Harvard's Robert F. Kennedy Award for Public Service and Stanford's Lloyd W. Dinkelspiel award for Outstanding Public Service.

Paavo Monkkonen, Associate Professor of Urban Planning — UCLA Luskin School of Public Affairs. Mr. Monkkonen's scholarship ranges from studies of large-scale housing finance programs to land use regulations and property rights institutions often not recognized for their importance to housing. His comparative research on socioeconomic segregation and land markets is broad ranging, spanning several countries including Argentina, Brazil, China, Hong Kong, India, Indonesia, and the United States. He continues to work as a consultant on national housing and urban policy in Mexico, where he has various longstanding research projects and teaches courses on housing markets and policy, applied microeconomics, research methods, and global urban segregation. He is also the coordinator of the Regional and International Development Concentration and a Faculty Cluster Leader for the Global Public Affairs Initiative. Mr. Monkkonen researches and writes on the ways policies and markets shape urban development and social segregation in cities around the world.

Mr. Monkkonen's research has been published in journals such as the Journal of the American Planning Association, the International Journal of Urban and Regional Research, the Journal of Urban Economics, Regional Science and Urban Economics, Urban Studies, World Development, and the Journal of Peasant Studies. In recent years, Mr. Monkkonen has received research funding from the John D. and Catherine T. MacArthur Foundation, the Regional Studies Association, the Lincoln Institute of Land Policy, the UCLA Ziman Center, the UCLA Asia Institute, the Global Development Network, and the Inter-American Development Bank. Mr. Monkkonen completed a Master of Public Policy at the School of Public Affairs at the University of California, Los

Angeles, and a PhD in City and Regional Planning at the University of California, Berkeley. He was previously Assistant Professor of Urban Planning at the University of Hong Kong from 2009 to 2012.

Laura Archuleta, President — Jamboree Housing. Since 1999, Laura Archuleta has guided Jamboree Housing Corporation from a small, Irvine, CA-based nonprofit affordable housing developer with 750 homes into the fifth largest nonprofit developer in California having developed 8,310 homes in more than 88 communities. Under Ms. Archuleta's leadership, Jamboree creates healthy communities where residents thrive as they live, work, shop, and play in their local neighborhoods. Ms. Archuleta was also instrumental in establishing Jamboree's in-house Community Impact Group, in 2004. In 2010, Jamboree expanded the Community Impact Group with the acquisition of HOMES, Inc., a leading nonprofit provider of housing and support for people living with mental illness. This partnership furthers Jamboree's goal to designate at least 10% of the apartment homes at each of its new properties to people with special needs. In 2012 Jamboree launched its own in house construction group, Quality Development and Construction, Inc. to ensure construction standardization across Jamboree's asset portfolio, as well as more cost-effective design solutions and greater sustainability to maintain affordability vital to Jamboree's commitment for the long term. Ms. Archuleta's advocacy has led to the production and preservation of more than 10,000 high quality homes for lower income families and seniors. Since joining Jamboree, she and her management team have grown the company's asset portfolio to a market value of nearly \$1.1 billion, directly benefiting more than 18,500 Californians.

Valerie Feldman, Staff Attorney — Public Interest Law Project. Ms. Feldman recently joined Public Interest Law Project's (PILP) staff after focusing on land use and housing issues at Legal Services of Northern California's Sacramento office for more than a decade. Ms. Feldman has pursued advocacy and litigation in multiple areas, including the preservation of federally subsidized housing, promoting and defending inclusionary zoning, housing element enforcement, fair housing, redevelopment law, the rights of public housing tenants, SRO residents, and tenants in condominium conversion properties. Ms. Feldman graduated from UC Davis School of Law in 2000 and now teaches an elective course there on housing law. She has served on the boards of the Legal Aid Association of California and Housing California, and currently serves on the board of the Sacramento Housing Alliance.

Shamus Roller, Executive Director — National Housing Law Project. Mr. Roller is the Executive Director of the National Housing Law Project (NHLP) which is a national, nonprofit housing and legal advocacy center established in 1968. NHLP advances housing justice by strengthening and enforcing the rights of tenants, increasing housing opportunities for underserved communities and preserving and expanding the nation's supply of affordable housing. Before joining NHLP in 2016, Mr. Roller served as the Executive Director of Housing California, a statewide advocacy organization working on issues of housing and homelessness. He started his career running street outreach programs for homeless youth, ran a meditation and yoga program for youth incarcerated in juvenile halls and was a practicing attorney. Mr. Roller received his B.A. in history from Reed College in Portland, Oregon and J.D. from the University of California, Hastings College of the Law in San Francisco.

Jeff Buckley, Senior Advisor on Housing Policy – Office of San Francisco Mayor Edwin M. Lee. Jeff Buckley is Senior Advisor to San Francisco Mayor Edwin M. Lee on housing policy. Since 2012, Mr. Buckley has been involved in crafting a number of housing policy initiatives including

the Mayor Lee's goal to produce 30,000 units of new housing by 2020 with 10,00 units affordable to low and moderate income residents. In 2012 after the dissolution of the state redevelopment agencies, Mr. Buckley helped lead the Mayor's 2012 Housing Trust Fund - a voter approved 30-year \$1.3 billion set aside for affordable housing. After federal sequestration reduced federal funding for public housing, Mr. Buckley helped implement Mayor Lee's Public Housing Re-Envisioning reform which, in partnership with the federal Housing and Urban Development Department, led to a \$2.2 billion effort to refinance, repair and rehabilitated 3500 distressed public housing units across the city. Mr. Buckley was also lead staffer on 2015 Proposition A – the city's \$310 million housing bond which helped to implement the mayor's ambitious housing goals. For nearly five years he represented the Mayor on the Executive Board of the Association of Bay Area Governments. Before joining the Mayor's Office, Mr. Buckley spent nearly 9 years doing social services, community and economic development work in San Francisco's Tenderloin neighborhood.

Oscar Wei, Senior Economist — California Association of Realtors. Oscar Wei is a Senior Economist at the California Association of REALTORS (C.A.R.), a statewide trade organization of real estate professionals with more than 180,000 members. Mr. Wei has been with the Research and Economics Department of C.A.R. since 2003. As an economist at C.A.R., Mr. Wei analyzes housing market conditions, consumer behaviors, and public policy issues through the use of survey research studies conducted by C.A.R. He assumes the responsibility on the compilation and the analysis of housing market data released to the public on a regular basis. He also contributes frequently to C.A.R.'s Market Analysis Articles, Housing Matters Blog, and Market Snapshot, and has written various topics including housing inventory, distressed sales, conforming loan limits, housing tax credits, housing affordability, and many other subjects relevant to the real estate industry. Mr. Wei has a Bachelor's degree in Economics from the University of California, Berkeley and a Master's degree in Economics from the California State Polytechnic University, Pomona. Prior to joining C.A.R., Mr. Wei worked for a toy company as an analyst to conduct research on identifying kids' trends and evaluated the global implication they may have on the toy industry.

Pete Parkinson, President — California Chapter of the American Planning Association. Mr. Parkinson is an independent planning consultant and President of the California Chapter of the American Planning Association. He served as planning director for the County of Sonoma until his retirement in 2013. Mr. Parkinson has worked as a professional planner and manager for over 30 years. Mr. Parkinson has long been active in planning policy issues, including representing the California State Association of Counties (CSAC) and APA California on various working groups. He served as Vice-President for Policy and Legislation with APA California from 2005 through 2010, and as President of the California County Planning Directors Association in 2005-06. In 2009, he was appointed by the California Air Resources Board to serve on the Regional Targets Advisory Committee to advise the ARB on setting regional greenhouse gas reduction targets under SB 375. Mr. Parkinson is a member of the American Institute of Certified Planners (AICP) and a graduate of the University of California, Santa Cruz.

Michael Battaglia, Vice President Project Development — CalAtlantic Homes. Michael Battaglia was elected by the CBIA Board to serve as the organization's 2017 Vice Chair. Prior to taking this role, he served in a variety of leadership positions at CBIA including President of the Building Industry Association of Southern California (BIASC) 2015 and 2016, Chair of the Political Action Committee for BIASC from 2013 to 2015, President of the Los Angeles County East Chapter of BIASC in 2006, and CBIA's Vice Chair of the Governmental Affairs Committee

in 2016. Mr. Battaglia joined Standard Pacific in June, 1998, as a Project Manager. In 2000, he was promoted to Director of Forward Planning, and in 2003, became Vice President Project Development. As Vice President, his duties include acquisition due diligence, land entitlements, governmental and political relations and managing the project management team that cover Los Angeles and Orange Counties for CalAtlantic Homes. Over the past 19 years with Standard Pacific/CalAtlantic Homes, Mr. Battaglia has entitled over one thousand homes. Mr. Battaglia graduated from Cal Poly Pomona with a Bachelor of Science Degree in Finance, Real Estate and Law (FRL) with a concentration in Real Estate Brokerage and Development. Mr. Battaglia currently sits on the FRL Advisory Committee.

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