

JOINT OVERSIGHT HEARING

SENATE HOUSING COMMITTEE AND
SENATE GOVERNANCE AND FINANCE COMMITTEE

Addressing California’s Housing Shortage: How Can We Create Environments to Facilitate Housing Development?

Tuesday, March 5, 2019, 1:30 pm
State Capitol Room 4203
Sacramento, CA 95814

Background Information

Purpose of the Hearing

In the fall of 2018, the Senate Transportation and Housing Committee and the Senate Governance and Finance Committee held two joint hearings. The first, titled “Housing for Working Families: How Do We Pay for It?” was held on October 2nd in Sacramento and assessed current state and local funding sources for affordable housing, identified funding gaps, and began to discuss the need for additional legislative changes beyond funding to address the state’s housing crisis. The second, titled “California’s Affordable Housing Crisis: Tailored Solutions to the Land Use Conundrum in Communities Big and Small” was held on November 16th in the City of Los Angeles. Building on the first hearing, that hearing examined changes to land use policies that are needed to increase density and challenges facing different areas of the state. Materials for those hearings are available on the Senate Housing and Senate Governance and Finance websites.

Today’s hearing, a joint hearing of the new Senate Housing Committee and the Senate Governance and Finance Committee, continues this conversation. This hearing will shed light on barriers to housing development, such as restrictive land use and approval processes, and seek solutions to mitigate the housing shortage in California as well as identify ways to encourage housing construction.

California’s Housing Shortage

California is in the midst of a serious housing crisis. California is home to 21 of the 30 most expensive rental housing markets in the country, which has had a disproportionate impact on the middle class and the working poor. Housing units affordable to low-income earners, if available, are often in serious states of disrepair. A person earning minimum wage must work three jobs on average to pay the rent for a two-bedroom unit. HCD estimates that approximately 2.7 million lower-income households are rent-burdened (meaning they spend at least 30 percent of their

income on rent), 1.7 million of which are severely rent-burdened (spending at least 50 percent of their income on rent).¹ Not a single county in the state has an adequate supply of affordable homes. According to a 2015 study by the California Housing Partnership Corporation, California has a shortfall of 1.5 million affordable homes and 13 of the 14 least affordable metropolitan areas in the country.²

A major factor in this crisis is the state's housing shortage. From 1954-1989, California constructed an average of more than 200,000 new homes annually, with multifamily housing accounting for the largest share of housing production. Since then, however, construction has dropped significantly. The state Department of Housing and Community Development (HCD) estimates that approximately 1.8 million new housing units – 180,000 new homes per year – are needed to meet the state's projected population and housing growth by 2025. Even when housing production rose in the mid-2000's, it never reached the 180,000 mark, and over the last 10 years construction averaged just 80,000 new homes per year.

In order to address the housing shortage, the state has undergone tremendous efforts to facilitate housing production. The housing package of 2017 made an effort to promote higher density housing, streamline housing approval processes, and increase zoning for housing while providing more state enforcement power. Legislation in 2018 sought to further increase housing production by reforming the RHNA process and ensure that every city and county is doing its part to provide housing for Californians. Despite these efforts, further coordination between the state and local governments is crucial to efficiently create housing. Planning and approving new housing is mainly a local responsibility, therefore, understanding these processes and identifying gaps where the state can intervene to improve and better aid local governments in their efforts is critical to alleviating the state's housing shortage.

The Role of Local Government

The California Constitution allows cities and counties to “make and enforce within its limits, all local, police, sanitary and other ordinances and regulations not in conflict with general laws.” It is from this fundamental power (commonly called the police power) that cities and counties derive their authority to regulate behavior to preserve the health, safety, and welfare of the public—including land use authority.

¹ California Department of Housing and Community Development, *California's Housing Future: Challenges and Opportunities, Final Statewide Housing Assessment 2025* (February 2018) at http://www.hcd.ca.gov/policy-research/plans-reports/docs/SHA_Final_Combined.pdf.

² California Housing Partnership Corporation, *Update on California's Affordable Housing Crisis* (April 2015) <http://chpc.net/dnld/2015StatewideHousingNeedReportFINAL.pdf>

General Plans Establish Allowable Intensity of Development. State law provides additional powers and duties for cities and counties regarding land use. The Planning and Zoning Law requires every county and city to adopt a general plan that sets out planned uses for all of the area covered by the plan. A general plan must include specified mandatory “elements,” including a housing element that establishes the locations and densities of housing, among other requirements. Cities’ and counties’ major land use decisions—including most zoning ordinances and other aspects of development permitting—must be consistent with their general plans. The Planning and Zoning Law also establishes a planning agency in each city and county, which may be a separate planning commission, administrative body, or the legislative body of the city or county itself. Cities and counties must provide a path to appeal a decision to the planning commission and/or the city council or county board of supervisors.

Zoning Ordinances More Precisely Shape Development. Local governments use their police power to enact zoning ordinances that shape development, such as setting maximum heights and densities for housing units, minimum numbers of required parking spaces, setbacks to preserve privacy, lot coverage ratios to increase open space, and others. These ordinances can also include conditions on development to address aesthetics, community impacts, or other particular site-specific considerations.

Local governments have broad authority to define the specific approval processes needed to satisfy these considerations. Some housing projects can be permitted by city or county planning staff “ministerially” or without further approval from elected officials, but most large housing projects require “discretionary” approvals from local governments, such as a conditional use permit or a change in zoning laws. This process requires hearings by the local planning commission and public notice and may require additional approvals. Still other projects may be permitted under a development agreement, which is a contract negotiated between a project proponent and a city or county. A development agreement governs the land uses that a city or county may allow in a particular project, as well as the fees and procedures that apply to the approval. Neither the applicant nor the public agency is required to enter into a development agreement; it acts as an alternative to the traditional approval process.

Barriers to Housing Development

A variety of causes have contributed to the lack of housing production, including restrictive zoning ordinances, local permitting processes that provide multiple avenues to stop a project, and fiscal incentives associated with development decisions. These issues pose challenges to constructing market-rate and affordable housing developments alike.

Restrictive Zoning Limits Housing Density. California’s high—and rising—land costs necessitate dense housing construction for a project to be financially viable and for the housing to ultimately be affordable to lower-income households. Yet, recent trends in California show that new housing

has not commensurately increased in density. In a 2016 analysis, the Legislative Analyst’s Office (LAO) found that the housing density of a typical neighborhood in California’s coastal metropolitan areas increased only by four percent during the 2000s.³ The LAO also compared California’s coastal areas to similar metropolitan areas across the country and found that new housing constructed during the 2000s in California’s coastal cities was nearly 30 percent less dense on average than new housing in other comparable cities—10 units/acre in California compared to 14 units/acre in the other metropolitan areas.

In addition, the pattern of development in California has changed in ways that limit new housing opportunities. A 2016 analysis by BuildZoom found that new development has shifted from moderate but widespread density to pockets of high-density housing near downtown cores surrounded by vast swaths of low-density single-family housing.⁴ Specifically, construction of moderately-dense housing (2-49 units) in California peaked in the 1960s and 1970s and has slowed in recent decades.

Zoning ordinances add additional constraints that can reduce density: setbacks, floor-area ratios, lot coverage ratios, design requirements, dedications of land for parks or other public purposes, and other regulations can reduce the space on a lot that a building can occupy in ways that lower the number of units it is feasible to construct on a lot. Local governments also sometimes establish stringent zoning restrictions specifically to maintain discretion over development.⁵ This practice allows them to bargain more effectively with developers for contributions to services in order to overcome the fiscal effects of residential development (discussed below), or to simply provide more opportunities to deny projects.

Permitting Processes Create Many Paths to Halt Projects. Recent reports point to the permitting and approval processes as a major factor preventing more housing construction. Local governments control most of the decisions about where, when, and how to build new housing, and those governments are quick to respond to vocal community members that may not want new neighbors. As described above, cities and counties often require multiple layers of approval for new housing projects and commonly include review by multiple departments within the city (such as the building department, fire department, and health department), a design review board, the planning commission, and the city council or board of supervisors. Many of these reviews must be conducted at public hearings, providing venues for residents that oppose development to make their voices heard. More complicated projects require even more approvals and procedural steps.

The building industry also points to environmental reviews and other permitting hurdles as a hindrance to housing development. They argue that the high cost of building and delays in the

³ Alamo, Chas and Brian Uhler. “California’s High Housing Costs: Causes and Consequences.” Legislative Analyst’s Office, March 2015.

⁴ Romem, Issi. “America’s New Metropolitan Landscape: Pockets Of Dense Construction In A Dormant Suburban Interior.” BuildZoom, February 2018.

⁵ Manville, M. and Osman, T. (2017), Motivations for Growth Revolts: Discretion and Pretext as Sources of Development Conflict. *City & Community*, 16: 66-85.

approval process reduce builders' incentives to develop housing. Each review or approval examines an important facet of a project, and the options of appealing decisions or challenging them in court ensures due process for developers and residents alike. However, these steps also provide many ways to stop or delay projects.

Fiscalization of Land Use. A series of propositions have drastically cut into local revenue sources, requiring local governments to look elsewhere to fund services that the public demands. First, Proposition 13 (1978) capped property tax rates at one percent of assessed value (which only changes when ownership changes) and required 2/3rds voter approval for special taxes; as a result, local governments turned to general taxes to avoid the higher voter threshold. When Proposition 62 (1986) required majority voter approval of general taxes, local governments imposed assessments that were more closely tied to the benefit that an individual property owner receives. Subsequently, Proposition 218 (1996) required voter approval of parcel taxes, assessments, and property-related fees.

In response to the reduction in property tax revenues from Proposition 13 and the difficulty of raising taxes, local governments have turned to other sources of funds for general operations, including sales taxes and hotel taxes. These taxes are paid exclusively by commercial developments, which simultaneously pay property taxes and demand relatively few services (such as public safety or parks). Residential developments, by contrast, do not directly generate sales or hotel tax revenue, and the new residents demand a wider variety of more intensive services. As a result, cities and counties face a disincentive to approve housing because of the higher net fiscal cost of residential development, particularly if they have the option to instead permit commercial development that may produce net fiscal *benefits*.

Effects of Restrictive Land Use Policies

The consequence of the above barriers is that housing production has not kept up with the increase in population in many parts of California. For example, between 2010 and 2015, the City and County of San Francisco permitted one new housing unit for every 8.2 new jobs; throughout the entire Bay Area, local governments permitted one unit for every 6.8 jobs.⁶ As a result, land use restrictions can have various negative consequences, such as increased displacement and segregation, as well as lower economic growth.

Displacement and Segregation. Stricter land use controls are also associated with greater displacement and segregation along both income and racial lines. Past practices such as redlining, which led to the racial and economic segregation of communities in the 1930s, have shown the negative effects that these practices can have on communities. The federal National Housing Act of 1934 was enacted to make housing and mortgages more affordable and to stop bank foreclosures

⁶ Salvati, Chris. "Housing Shortage: Where is the Undersupply of New Construction Worst?" *Apartment List*, July 2017.

during the Great Depression. These loans were distributed in a manner to purposefully exclude “high risk” neighborhoods composed of minority groups. This practice led to underdevelopment and lack of progress in these segregated communities while neighborhoods surrounding them flourished due to increased development and investment. People living in these redlining communities had unequal access to quality, crucial resources such as health and schools. These redlined communities contain higher minority and poverty rates today and are experiencing gentrification and displacement at a higher rate than other neighborhoods. Today, exclusionary zoning can lead to “unintended” segregation of low income and minority groups, which creates unequal opportunities for Californians of color. Both the LAO and an analysis by the Institute of Governmental Studies (IGS) at the University of California, Berkeley indicate that building new housing would reduce the likelihood that residents would be displaced in future decades.⁷

Lower Economic Growth. Restrictive land use policies also hurt economic growth more broadly because they keep residents from moving to more productive areas where they can take more productive jobs that pay higher wages. For example, one analysis found that highly productive cities in the United States have not contributed to economic growth as much as their productivity would imply because of housing constraints that keep workers from those cities, and that gross domestic product (GDP) could be as much as 9.5 percent higher if those constraints were relaxed.⁸ Other scholars argue that low-density zoning also hurts the regional economy: there is some indication that housing costs have pushed startups from California to other states, and have driven some companies, such as Toyota, to relocate out of California.⁹

State Housing Law

State law requires local jurisdictions to plan for their future housing needs, as determined through the regional housing needs allocation (RHNA) process. Under RHNA, the Department of Finance and HCD develop forecasts of the number of housing units at various income levels needed to keep pace with population growth, which they allocate to regions throughout the state. Regional “councils of governments” allocate the regional housing need to local governments within those regions, which must develop a plan – the housing element portion of their general plan – to accommodate the additional housing growth. During the most recent housing element cycle, not a single region built sufficient housing to meet its regional housing need. For example, of the two most populous regions of the state, the Southern California Association of Governments region produced 46 percent of its respective need and the Association of Bay Area Governments produced 53 percent of its need. Statewide, only 47 percent of the housing required to meet projected need

⁷ Zuk, Miriam and Karen Chapple. “Housing Production, Filtering, and Displacement: Untangling the Relationships.” Institute of Governmental Studies, University of California, Berkeley, May 2016.

⁸ Hsieh, Chang-Tai and Moretti, Enrico, “Why Do Cities Matter? Local Growth and Aggregate Growth.” *Kreisman Working Paper Series in Housing Law and Policy*, 2015.

⁹ Monkkonen, Paavo. “Understanding and Challenging Opposition to Housing Construction in California’s Urban Areas.” *UC Center Sacramento Housing, Land Use and Development Public Lectureship and White Paper Award*, December 2016.

was constructed during this period. This is due in part to the limited ramifications communities have faced if their housing element is not approved by HCD; to address this problem, the Legislature passed a number of bills last year aimed at strengthening housing element law.

Conclusion

Policy solutions must ensure that all communities across the state do their part to address the housing crisis. These solutions may include policy changes, financial incentives, state investments, and a successful path forward will include both carrots and sticks to encourage cities and counties to permit housing—some of which will be unpopular among local officials and others that will be welcomed. Furthermore, members of the Senate will have an opportunity to identify solutions through the policy process, as well as the Governor’s proposed housing and homelessness budget. A successful approach will combine funds for affordable housing to immediately produce housing needed for the most vulnerable Californians, along with steps that increase market-rate housing production to prevent the crisis from worsening and to reduce rents in the long term.