



BRIEFLY

Many areas of Washington State are experiencing a housing supply crisis, with the homebuilding industry unable to keep up with demand, and prices rising by double-digit rates. State policies helped create this situation and it is incumbent on the state to take action to remedy it.

Ways to Boost Housing Supply: *State Actions*

There is no question that Washington State has a major housing supply problem, with the homebuilding industry unable to keep up with demand in the moderate and lower cost ends of the market. This brief outlines ways that action at the state level can help remedy the situation. While most plans and regulations that govern homebuilding are made at the local level, the framework for those plans and regulations is created by the state. State policies and laws that clearly encourage housing production will make it easier for advocates at the local level to ensure that city and county policies do the same.

INCREASING HOUSING SUPPLY: CAPACITY AND EFFICIENCY

The third brief in this series described the two basic ways to address the housing supply problem (Washington Research Council 2006a). The first way is to make the industry more responsive to increases in demand, so that greater demand triggers a sharp increase in supply with only modest price increases. The goal is to have the housing industry respond to price signals by having existing builders quickly expand production and have new builders jump into the market.

The second way to increase the amount of housing on the market is to allow the homebuilding industry to be more productive and efficient, so that the cost of producing housing falls. The goal is to foster structural changes in the housing industry that allow builders to produce housing more cost-effectively.

A combination of these two forces – a housing industry that is able to be more responsive to demand and more efficient at production – would have the effect of keeping housing prices flat. This can happen, as seen in the Atlanta region, where population has grown substantially, while housing prices have increased only at the rate of inflation.

As shown by Glaeser and Gyourko (2003), the real culprit in high housing prices – which are a reflection of inadequate supply – is the cost of getting land permitted for construction. Although recent increases in materials costs will have some impact on prices, construction costs have actually been increasing at less than the rate of inflation, and does not vary greatly across markets. Table 1 shows the per square foot

GIVE'EM SHELTER

A five-part series examining the availability and affordability of housing in Washington State.

Part 4



Table 1: Residential Construction Costs

	Average Two Story House Construction Cost per Square Foot		
	2000	2005	Avg. Annual Increase
	Seattle	\$71.26	\$77.82
Tacoma	\$74.78	\$76.75	0.5%
Olympia	\$74.78	\$76.75	0.5%
Vancouver	\$78.31	\$74.45	-1.0%
Wenatchee	\$66.32	\$69.08	0.8%
Yakima	\$73.37	\$72.91	-0.1%
Spokane	\$71.26	\$76.75	1.5%

Source: R.S. Means Residential Cost Data

cost of building an average two story home in various parts of Washington in 2000 and in 2005. With only construction costs increasing slowly, the large recent spike in housing prices must reflect a scarcity of building sites.

The key to more demand-responsive and cost-effective home construction lies in the ease of land development. If raw land can be turned into building lots or multi-family sites quickly, and if the cost of those sites or lots stays low, then housing supply can grow to meet demand at reasonable prices. State policies can help make this happen. Still, many of the solutions dis-

ussed below require implementation at the local level, as will be discussed in the next brief in this series (Washington Research Council 2006b).

MAKE HOUSING A PRIORITY

Before specific policy prescriptions can become a reality, housing supply must become a higher priority for state government. Expanding the housing supply represents a competing use for land and infrastructure funding and challenges existing regulatory frameworks. Under current legal and policy conditions, increasing the housing supply in an amount sufficient to hold down prices will not happen by accident. It will take a specific commitment and a willingness to trade off other values. In other words, housing supply is a political, and not just a technical problem.

In many of the policy regimes that affect housing, the default position is unfriendly to new housing supply. For example, the Growth Management Act (GMA) specifically requires the preservation of farmland and resource lands, but leaves housing supply as one of thirteen unprioritized goals. So, while local governments are required by state law to save as much farmland as possible, they are not required to provide enough housing to meet the demands of job growth.

Similarly, transportation funding is geared heavily toward preservation and enhancement of existing systems, and not toward providing new capacity to growing areas. This may be helpful for infill areas, but hinders the ability of outlying areas to absorb growth. Given the poor condition of much of the state's road and highway network, this policy could steer nearly all available road funds toward maintaining the existing system, making it impossible to open new housing developments.

Housing will always face a number of political dilemmas. First, most voters already have homes and therefore do not see a need to pressure elected officials to create more housing. Second, housing policies have only an indirect impact on construction, so their efficacy is never certain. Governments do not build housing, but rather create the environment within which the homebuilding industry operates, so government action cannot guarantee more housing. Third, housing policies take a long time to show results. Planning and infrastructure investments roll out over years, even decades, making it difficult to draw a direct line between a vote taken by an elected official and a new home enjoyed by a constituent.



State government faces a fourth political challenge in navigating its complex relationship with local government. Land use regulation has always been a carefully guarded prerogative of local government, and the legislature will hesitate to interfere too much in local decision-making. Growth management changed the state-local relationship, but after 15 years, the interaction of state and local goals remains murky.

For new housing supply to truly become a priority for state government, legislators and the governor need to overcome these political hurdles. If the supply remains inelastic, higher housing prices will gradually squeeze moderate income-households out of the state's most prosperous urban areas.

BRINGING IN NEW SUPPLY: LAND AVAILABILITY AND CAPACITY

The ultimate decisions about the supply of land available for building housing, and the capacity of that land, are made by local governments. State policy can, however, have a major influence on what local governments do. The following are issues and recommendations for action at the state level.

Problem: overestimating land capacity

The second brief in this series provided an extensive discussion of the Buildable Lands process and the tendency to overestimate the capacity of the land currently available for development within urban growth areas (Washington Research Council 2005c).

Because urban growth lines are fixed, and because land within those lines is being developed at a steady pace, the supply of available land is constantly shrinking. The owners of that land are confident that demand for housing will continue to grow, so they will keep asking higher and higher prices for their land. And as land prices increase, builders cannot justify using expensive land for the moderately-priced housing that makes up the bulk of new supply. Thus, an inadequate land supply means that an increase in housing demand will result in mainly an increase in production of expensive housing.

Solution: reform the Buildable Lands process

As discussed in the previous brief, the Buildable Lands processes undertaken a few years ago do not provide enough information to policy-makers to help them ensure that the supply of land is adequate to meet growth needs. Because the Central Puget Sound Growth Management Hearings Board has ruled that the King County process followed the letter of the law, it is clear that the law needs to change. The Buildable Lands statute should be amended to:

Ensure more input and accountability. The statute now treats the Buildable Lands process as a purely technical exercise, and therefore provides no formal avenues for public input or accountability by elected officials. There is, however, significant room for judgment, and the process requires policy decisions about assumptions and methodology. There should be room for public input on these. Moreover, the final product should be endorsed and approved by the city or county council, so there is a higher level of accountability. Too much is at stake for the Buildable Lands process to take place in a black box.



Factor in infrastructure investment plans. Areas not currently served by infrastructure can be counted as “buildable” with no regard to whether infrastructure will be funded in any reasonable timeframe. Capital improvement plans typically stretch out no more than six years, so there is no way to know if a non-served area can be considered “buildable” in a practical sense (i.e. served by water, sewer and adequate roads) within the timeframe of the comprehensive plan.

The Buildable Lands statute should be amended to require jurisdictions to account for two types of land: that served by infrastructure now or within the current capital improvement plan (CIP), and that not served now or in the current CIP. No jurisdictions should be allowed to count non-served land as part of its core land capacity (i.e. that needed to meet housing targets). As CIPs roll over and new projects are added, land that will be served can be shifted over to the core capacity.

Require a realistic market factor. When all the vacant and redevelopable land is added up, the total is reduced by a “market factor” that recognizes that some land will not come on the market during the planning period. Currently, jurisdictions arrive at a market factor through guesswork, resulting in market factors ranging from five percent to 25 or 30 percent. This discount factor is too important to be left to chance.

A more realistic market factor could be arrived at through a survey of property owners to determine their willingness to sell their land, and the prices they expect to get. Such a survey should include owners of both vacant and redevelopable land, since land with an existing use is less likely to be put on the market than vacant land. The Buildable Lands statute could be amended to require that a land market survey be conducted on a county-wide basis with substantial private sector input. All jurisdictions in the county would use the information from the survey to derive their own market factors, which should be quite similar.

Account for consumer preferences. Currently, capacity is considered adequate if it provides for the required number of housing units, without regard to what sorts of housing types might be desired in the area. Although preferences are shifting, there is still substantial demand for single family detached and semi-detached housing. The Buildable Lands reports should be clear about whether there is enough capacity for those types of housing to meet the demand that would arise from projected population growth.

The Buildable Lands statute could be amended to require that an assessment be conducted of the anticipated demand for various types of housing. Since housing markets tend to overlap city boundaries, market studies could be conducted on a market-area basis, rather than on a jurisdiction-by-jurisdiction basis. The capacity for various types of housing, by zoning category, can then be compared to that assessment to determine if there is sufficient capacity to meet consumer preferences. The comparison of capacity to demand will also indicate if a jurisdiction is relying on a type of development that is not likely to take place.

Provide a larger cushion of surplus capacity. To be considered adequate, the capacity of buildable land can be exactly the amount needed to meet housing targets. Cutting the supply this close leaves no room for error in measurement or projections, and does not allow for accommodation of an unexpected surge in demand. Moreover, market behavior suggests that as land is used up and the supply becomes tighter, prices will increase.



A mandatory cushion should be required for each housing type or zoning category within each jurisdiction. A cushion of 25 to 50 percent would ease pressure on the market while still promoting infill development. And, it would allow some infill land to remain undeveloped and banked for unknown future uses.

Larger market factors for small parcels. Small parcels are less likely to be developed than larger ones, especially if they are redevelopment sites with a current use. For example, a double lot with an existing house is not likely to attract commercial developers, and the owner may not be willing to develop it into a building site. Although such parcels are measured as “buildable” in the same way that larger parcels are, they can remain undeveloped indefinitely.

The discounting process that includes the market factor should include an additional factor for the lower development rate of small parcels. It would be prudent to create a discounting factor for small parcels that is double the market factor used for the zoning category. For example, if a 20 percent market factor is applied to single family zones (i.e. 80 percent of vacant or redevelopable single family land is expected to come on the market during the planning period), a factor of 40 percent would be applied to single family parcels yielding four units or fewer.

Provide more effective remedies for deficiencies. If, after the Buildable Lands process is complete, a jurisdiction finds that it is not meeting its density goals and/or does not have adequate capacity to meet targets, it is required to take measures “reasonably likely” to improve the situation. This process needs to be strengthened in order to provide better results.

The “reasonable measures” section of the Buildable Lands statute would benefit from three changes. First, it should be triggered more readily, based on a lack of cushion (see above) rather than an actual deficit of capacity. Second, only measures that will have very direct results should be accepted (e.g. rezones for high-demand housing types). Third, the effectiveness of the measures should be evaluated in a timely way, so that new measures can be taken if the initial measures prove ineffective.

The reforms to the Buildable Lands process outlined above will almost certainly result in the need to add homebuilding capacity in many jurisdictions. This will likely need to be done by some combination of rezoning and/or expansion of urban growth areas. Any such rezones or UGA expansions must, however, be consistent with anticipated demand for various housing types. Adding capacity for low-demand products will not help.

Problem: missing the market upswing with slow permitting

Normally, demand in the housing market tracks business cycles. When the economy picks up, in-migration increases and higher incomes allow more people to upgrade their living situation. The degree to which an increase in demand puts pressure on prices depends on the speed that new housing can be produced to satisfy that new demand.

The challenge in meeting new demand is that business cycles can shift much faster than the housing industry can gear up production. It usually takes years to get a subdivision approved and turned into building lots with roads and utilities, and then another year or so to build homes on those lots. When an economic downturn appears on the horizon,



land development permitting activity slows down, since no one wants to get stuck with unsold lots when the downturn hits. Then, when the recovery comes, there is nothing in the pipeline.

Multifamily construction follows a similar pattern. At the first sign of a downturn, investors cool on the idea of committing to new building projects, and the pipeline of new apartments and condominiums dries up. When the recovery comes, there is a surge of construction, but multifamily construction can also take years from initial concept to finished units.

Solution: faster permitting of subdivisions and multifamily projects

The speed of permitting processes is a large and well-worn topic, but it is frequently discussed in terms of the added costs that burden the project through delays and additional design and engineering fees. Faster permitting will affect housing costs on the demand side as well, by closing the lag time between a demand increase and the availability of new supply.

While the efficiency of most permitting processes is a function of local government, state government can have a big impact. First, permit processing timelines need to be reinstated and strictly enforced. While not all jurisdictions complied with state-mandated permit processing times, and there were large loopholes in the mandate, the time limits did focus local governments on reforms to their permitting agencies.

Second, much of the land development permitting process involves compliance with state laws, such as the State Environmental Policy Act and the Shorelines Management Act. There is further need to streamline these laws and address the overlap between them and the Growth Management Act.

Problem: developable land not served by infrastructure

If land that should be available for development is not currently served by urban-level infrastructure (water, sewer, roads) it cannot be developed easily. In some cases, areas are large enough that developers are willing to spend their own money on infrastructure extensions (e.g. freeway interchanges serving Issaquah Highlands and Northwest Landing) but smaller projects, which make up the bulk of land development, cannot undertake major infrastructure extensions on their own.

Land development, and therefore housing construction, will happen much faster if major infrastructure is in place before the land is needed. But this rarely happens. For decades, infrastructure capacity has not kept up with growth, and maintenance has not kept up with aging of systems, so the vast majority of infrastructure spending must go to catch-up on capacity expansion and maintenance in already-developed areas. This leaves little money available to provide new infrastructure to areas slated for future development.

Solution: provide road funding for growth areas

The state has a large role in the planning and financing of the road and highway systems needed to accommodate housing growth (the state has much less of a role in water and sewer systems). Priorities will always be with maintenance of the existing system and with expansion in con-



gested areas. But the state should set aside funding – in both state highway accounts and Transportation Improvement Board accounts – for capacity improvements to areas expected to accommodate growth. A base of state dollars will provide the impetus for local governments and private developers to round out the funding for growth-related projects.

The state should begin to adopt the principle that growth does pay for itself. Currently, the state charges sales tax on all commercial, residential and institutional construction projects as well as most purchases of business equipment and fixtures. These tax collections represent one-time revenue sources that are totally dependent on growth in housing and economic activity. They could be set aside, on a phased-in basis, to form a special fund for roads that serve newly-growing areas. With funds set aside, areas ready for development will not have to wait for some future promise of road funding and can enter the pipeline sooner.

BRINGING IN NEW SUPPLY: FACILITATING INFILL

With the exception of some central Puget Sound communities, urban infill has yet to make much of a dent in overall housing supply. But as land on the periphery of metropolitan areas becomes increasingly scarce and expensive, infill sites become more attractive. Infill does, however, remain a more expensive and complicated form of housing development. The advantage of infrastructure availability is offset by higher land and development costs, fewer economies of scale, and marketing problems.

Infill development is a central tenet of the Growth Management Act and a substantial part of the supply of new housing is expected to be built on infill sites. There are a number of ways the state can promote infill housing and help ensure that it contributes to the needed growth in housing supply.

Problem: existing zoning is not always best

Because they are surrounded by developed areas, infill sites have existing zoning. The uses and housing types allowed by that zoning may not, however, make the best use of the site. Different product types, often at higher densities, can provide a better fit for the neighborhood and better economics for the developer.

For example, in a neighborhood developed in the 1950s with 1,200 square foot homes, an infill project of large single family homes would not fit well and would be difficult to market. Allowing smaller lots and smaller homes in such a situation would make a better project for both the developer and the neighborhood.

Solution: performance-based zoning

Most zoning is based on lot size or density. But since the purpose behind zoning is to manage impacts, it can make more sense to look at a project in terms of how it affects the surrounding community, rather than just unit count. After all, a unit designed for a family with teenagers is going to have a much higher impact than a unit designed for a retiree.

The GMA could be amended to require that all cities and counties have in place a process to provide an alternative review of projects based on impacts. This might be similar to a planned unit development (PUD) process, but it must allow for higher unit counts, not just clustering.

The process would not supplant existing zoning, but would allow an alternative use, subject to certain conditions. The developer could choose this alternative with the understanding that the outcome might be less certain than if a project were pursued under existing zoning.

Problem: inadequate local infrastructure

One of the cornerstones of growth management is the idea that development should be channeled to areas with existing infrastructure, thereby making the most use of past investments. As it turns out, much of the infrastructure in areas that are ripe for infill is either too small, in poor condition, or both. Because infill development happens one parcel at a time, it is difficult to finance major upgrades.

This is a particular problem in low-density residential areas that have no sewers or sidewalks. Building sewer lines and upgrading streets to urban standards is very expensive, and current property owners will balk at paying for something they have learned to live without. As a result, infill areas with poor infrastructure can remain underdeveloped indefinitely.

Solution: value-capture financing of infrastructure

Value-capture refers to several financing techniques that allow communities to bootstrap their way to new infrastructure by using a portion of the increased value of properties that results from infrastructure investment. There are three common types of value capture, each with its own set of challenges (Washington Research Council, 2005a).

Tax increment financing (TIF). TIF uses the increase in property taxes collected on a parcel after development to fund the infrastructure needed to make that development happen. TIF is used widely in the United States to fund redevelopment of urban areas. In Washington State, however, TIF encounters constitutional issues, and, as such, the current statute has proved unattractive. Ultimately, it will require a constitutional amendment to allow effective TIF in Washington.

Local Improvement Districts (LID). These districts are created to fund improvements to a specific area. They allow the sale of bonds to pay for improvements, with the bonds paid off with a special property tax levy imposed on adjacent properties. Although cumbersome, LIDs are an excellent way to pay for improvements to an area that is built-out but ripe for redevelopment.

Latecomer processes. With a latecomer process, the first developer into an area pays the full cost of improvements such as sewer lines, water lines or street upgrades. Then, when later developments tie into the new facility, they reimburse the original developer for their share of the cost of the improvements. Latecomer processes can work well in cases where a single large developer, with deep pockets, kicks off redevelopment of an area.

There is a state role in strengthening each of these processes so that they can be used more widely to unlock development potential of infill sites for housing. Although attempts to amend the state constitution to allow TIF have failed in the past, the apparent willingness of state residents to invest in infrastructure may signal that it is time to try again. LIDs are currently allowed, but the process is considered very cumbersome, and could use some adjustments. Latecomer processes are also authorized, but not all local governments have them in place. The state



could require that all jurisdictions planning under GMA have latecomer processes available.

Problem: accessory housing remains underdeveloped

Accessory housing represents perhaps the greatest untapped source of new housing supply. Apartments built in basements, garages or as separate cottages in back yards can provide inexpensive, high quality housing in existing neighborhoods, while, at the same time, providing income for the property owner.

The GMA requires the larger jurisdictions planning under the Act to permit accessory housing, but allows local governments to write their own statutes, imposing whatever restrictions they feel to be necessary. As a result, many jurisdictions have overly-restrictive accessory ordinances that discourage development of this potential housing supply.

Solution: set parameters for accessory housing ordinances

The state's accessory housing law could be amended to set specific parameters that local governments must follow in drafting their accessory housing ordinances. Such parameters should allow for detached units, and set a generous maximum size. Additionally, there should be no restrictions on who can rent the unit. Local ordinances should also provide for administrative review of permits and not require them to be sent to city councils or planning commissions.

Problem: special districts not always cooperative

In many newly incorporated cities, fire districts and utility districts remain in place as separate governments. Although they provide crucial services and regulatory oversight, they cannot be compelled to cooperate with the plans and policies of cities. For example, fire districts review the emergency access features of new roads that are built in subdivisions and may not approve of innovative road designs that make more efficient use of land and provide more attractive streetscapes. Some utility districts impose very high hookup charges on new water and sewer lines, driving up the cost of lot development.

Solution: merge special districts into cities

Special districts, like cities, are creatures of state government, and therefore can be restructured by state action. The state could require that all utility and fire services within incorporated areas be provided by city departments. Districts that overlap jurisdictions could be broken apart or operated by one city through inter-local agreement. Districts could continue to operate in unincorporated areas, although it may make sense to have city utilities operate in those areas, as is often the case currently.

CONCLUSION: NO TIME FOR HALF-MEASURES

While the state does not process permits for subdivisions or apartment buildings, it does have significant influence over the supply of housing. The state has long provided the basic highway infrastructure that enables growth, and through the State Environmental Policy Act it asserted a larger role in shaping land use. The big change came when the legislature adopted the GMA and took a bold step toward leadership on a wide range of goals. But leadership means more than passing laws



and stepping back. The state needs to continually adjust its laws to ensure they are effective and productive, providing tools and infrastructure that local governments need to manage growth effectively.

Many areas of Washington State are experiencing a housing supply crisis, with the homebuilding industry unable to keep up with demand, and prices rising by double-digit rates. The impacts of this situation are significant, ranging from labor shortages and wage pressures to crowded freeways and poor air quality. State policies helped create this situation and it is incumbent on the state to take action to remedy it.

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