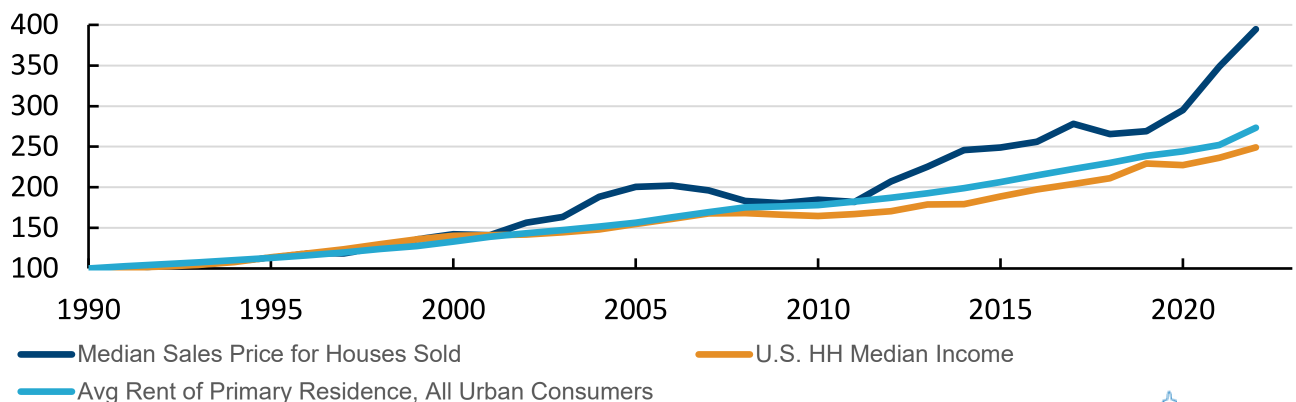
Rebuilding the American Dream: Policy Approaches to Increasing Housing Supply in the U.S.

A strong U.S. middle class depends on families having the opportunity to buy a home, build wealth and pass it on to the next generation. Research has shown that when low-income families move to stable homes in neighborhoods with a range of family incomes, their young children's future earnings and life outcomes improve significantly. Broad access to affordable and stable housing helps ensure Americans' economic well-being and mobility. However, the current housing shortage limits Americans' ability to access this next step.

Currently, middle-income households are struggling to secure affordable housing and homeownership is out of reach for many Americans. Rents have also been climbing over the past decade and many lower-income families are being priced out of their current neighborhoods. Meanwhile, these families are blocked from renting in higher income neighborhoods due to absence of smaller, more affordable housing options and housing discrimination.

Growth in Housing Prices Have Outpaced Growth in Median Income

Index where 100 = the value in January 1990



Source: The U.S. Census Bureau, the U.S. Department of Housing and Urban Development, and the U.S. Bureau of Labor Statistics

The United States has arrived at this moment after decades of exclusionary zoning and land use regulations that have limited housing choice and supply. Fortunately, states and localities across the country have been actively working to reverse this history, taking action to modernize their land use and zoning rules and enact new policies that build more housing that is accessible to a wider array of income levels. In addition to more better paying jobs and full funding for housing vouchers, which are vital to ensuring stable housing, these efforts to increase supply can help to relieve economic and housing capacity pressures from the housing shortage. Policy changes occurring across the country can serve as test cases for enhancing housing affordability and provide guidance for federal efforts to increase housing stock, while enhancing economic freedom.

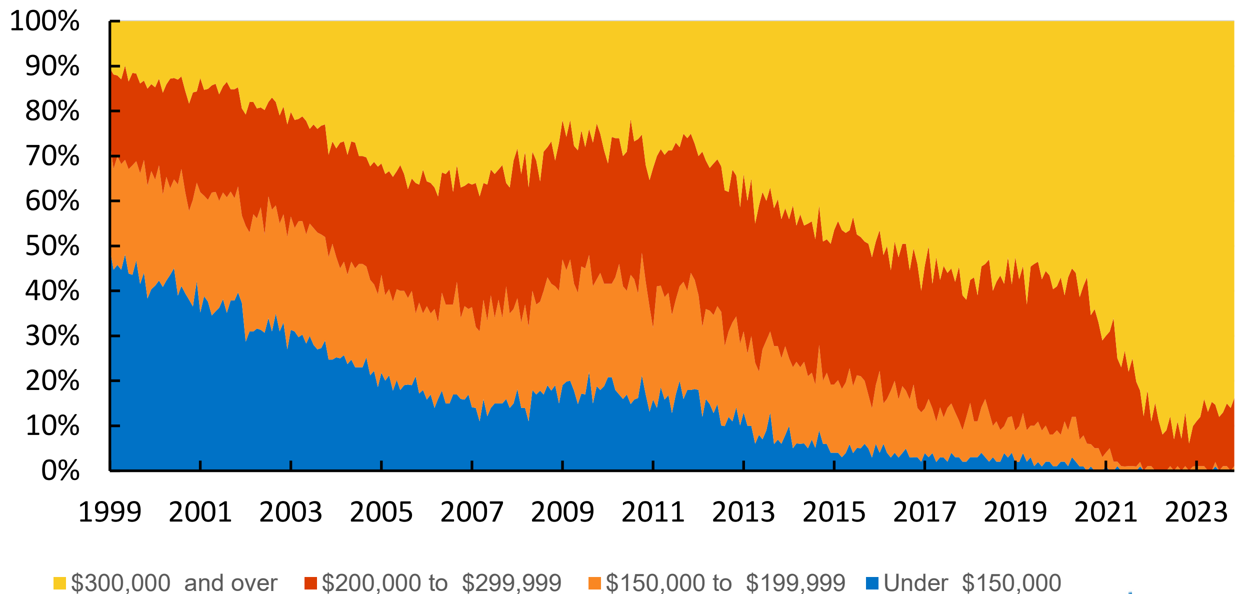
Removing Barriers to Housing Supply Can Enhance Affordability

Increasing housing supply to meet demand can help reduce growth in prices.

The U.S. is facing a housing affordability crisis driven in large part by inadequate housing supply. After the housing market collapse in 2008, new housing supply for single- and multi-unit buildings declined. Yet, as demand recovered, supply did not. Building on this crisis, in the wake of the pandemic the number of housing units available for purchase or for rent fell to near record lows. In 2021, Freddie Mac estimated that the shortage of newly-built homes was about 3.8 million, noting that entry-level starter home construction has fallen since the 1970s.

Few Homes are Constructed at Affordable Prices for Middle-Class Families

Percentage of new houses sold in the United States by sales price.

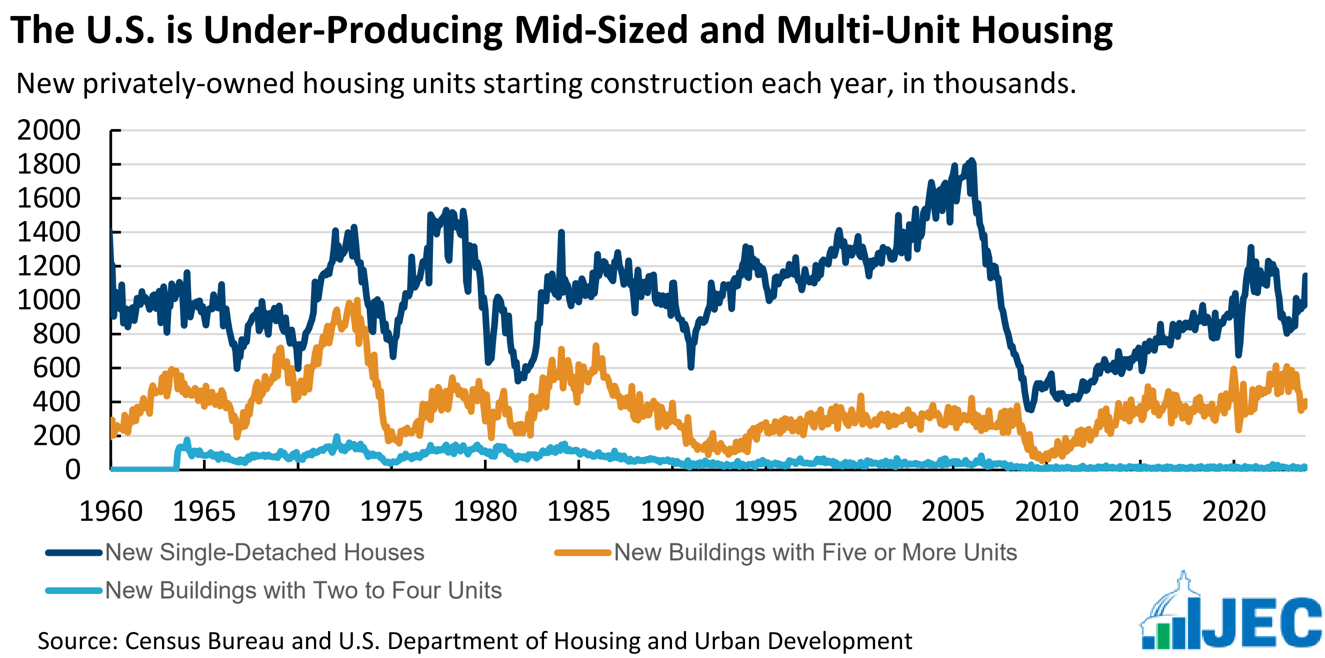


Source: Census Bureau and U.S. Department of Housing and Urban Development

The housing shortage is impacting affordability for renters and prospective homeowners alike. For example, in 2022 those earning at or below U.S. median income could only afford to own 20 percent of all homes on the market, down from about 50 percent in in 2016. Additionally, as the Council of Economic advisors wrote in 2021, “across the country, more than 10 million renters (one in four) pay more than half of their income on rent, and nearly half (47 percent) spend over the recommended 30 percent of their income on rent and utilities.” Research has shown that an increase in supply of housing stock can alleviate this upward pressure on home prices and help ensure that more affordable options are available to average Americans.

Zoning and land use regulations are making it more difficult to increase housing supply.

While increasing housing stock can help relieve the affordability crisis, zoning and land use regulations that mandate how land can be developed often actively prevent much-needed new housing construction. Many of these laws, which are implemented at the local or state level, directly restrict the number of units that a structure can have or limit the size of the structures through restrictions on square-footage, lot size, or height. These rules often mean that a single-detached home is the only type of housing that is legal to build in these areas. Meanwhile, other zoning and land use laws block construction of new housing altogether.



Many of these laws limit choice in housing type and location by barring construction of more affordable options like townhouses, duplexes, and smaller apartment buildings in favor of standalone single-family houses on larger lots. These mid-sized buildings, which can house between two to four families on a single lot, are still rarely built with developers mainly favoring single-detached houses or to a lesser extent, larger apartment buildings. Such restrictions on housing choice continue to place limits on who can afford to rent or purchase a home based on their income level.

Zoning and Land Use Regulations Are Maintaining Regressive Barriers to Housing Choice and Stability

While local and state laws currently govern zoning and land use, the federal government led in shaping exclusionary standards that are common throughout the country.

Historically, the federal government has given local governments the authority to set land use rules, while also acting as a guiding hand for what land use policy should look like throughout the country. Starting in the 1910s, an initial wave of state legislation gave municipalities zoning authority and established local planning boards. Then in the 1920s, the Department of Commerce (DOC) under Secretary Herbert Hoover issued guidance for legislative language for states to establish zoning authorities for general municipalities and cities. Researchers note that the DOC drafted this legislative language in order to provide a framework that minimized legal challenges to municipal zoning. Over time, all 50 states, and DC, adopted a form of these guidelines, and the American Planning Association found that many states continue to use laws based on these models today.

Exclusionary zoning limited housing supply and left a legacy of unequal opportunity.

Following these actions, restrictions on where people could live and the types of housing they could live in, laid the groundwork for the housing challenges the country faces today. For example, the boom in single-family detached housing developments in the 1940s, 50s and 60s coincided with a massive increase in homeownership. Yet the neighborhoods developed in this era were initially closed to families of color. Federal agencies refused to provide mortgage insurance and financing for homes in neighborhoods where primarily families of color lived, despite providing an abundance of such assistance to other families across the United States. Restrictive covenants also barred many families from homeownership, and real estate companies' discriminatory practices further limited housing choice.

While the Fair Housing Act outlawed many of these discriminatory practices in 1968, land use and zoning restrictions perpetuated inequality in housing access while maintaining the status quo of neighborhood segregation. For example, municipal governments enacted laws to rezone multiple residential neighborhoods for commercial use or construction of new highways, projects which were also funded by the federal government. These neighborhoods were primarily home to lower- and middle-income families and communities of color. Meanwhile, wealthier localities blocked new housing construction in neighborhoods with single-detached homes—the primary form of housing at the time—with new zoning and land use regulations. Taken together, such practices, through their legacy or continued use have played a large role in preventing economic and racial integration in many American neighborhoods, and in creating additional barriers to housing stability for more Americans.

Land use and zoning restrictions continue to limit housing stock and economic freedom.

Restrictions that limit where people can live have been found to harm the wider economy. Often, lower-income workers live further from job centers, in large part because housing in job-rich areas is too expensive for them to afford. In addition to impacting one's job and income prospects, a person's neighborhood often impacts their academic achievement and health, as well as that of their families and future generations. Studies have also linked restrictions on housing choice to lower levels of U.S. GDP.

Racial segregation by neighborhood also remains a reality in the United States. For example, research has shown that due to continued exclusionary zoning—which influences who can easily attend certain local public schools—school segregation today mirrors levels seen in 1968, the year that Congress passed the Fair Housing Act.

States and localities have started to enact laws that can help undo the harms of zoning and land use regulations, and build the foundation for more inclusive and affordable neighborhoods. These initial efforts can serve as models for future work across the United States.

State and Local Efforts Towards Zoning Reform Can Help Reshape the U.S. Housing Market

Despite the challenges presented by restrictive zoning policies, many states and localities are passing laws meant to modernize housing regulations and increase the number of housing options available to residents. Below are three examples of policy changes that take aim at the negative effects of past zoning rules.

Oregon: Reforming State Law to Increase Local Government Uptake of Zoning Reform

In 2019, Oregon became the first state to require that nearly all cities and towns change their zoning codes to allow for a wide range of housing options for families. The new law—House Bill (H.B.) 2001—requires every city with 10,000 people or more, as well as every city in the Portland metropolitan area with 1,000 or more people, to amend their zoning codes to allow for townhouses, duplexes, or other types of adjoined housing. About 70% of all residents of the state reside in an area that this law impacts.

Governor Tina Kotek—who championed the bill during her time as Oregon Speaker of the House—explained that the law was meant to re-establish economically-diverse neighborhoods that were ubiquitous in Oregon in the past. In contrast, at the time of H.B. 2001's passage, 77% of land in Oregon zoned for residential housing was restricted to single-detached houses. The state legislature will also be providing funding to assist localities in implementing the new zoning regulations to align with H.B. 2001. Governor Kotek has previously emphasized the impact of the law will be gradual, taking place over up to 20 years.

California: Using New and Existing Law to Expand Variety in Housing Structures, and Grow Supply

In 2021, Governor Gavin Newsom signed Senate Bill (S.B.) 9 into law, which legalized more housing choice throughout California. Homeowners now have more freedom and flexibility when it comes to how they use their property. The new law requires a simpler local government approval process for conversion of single-detached homes into duplexes, splitting a lot in two in order to build two smaller homes or duplexes, or adding a small accessory dwelling unit (ADU) to their land. This law led to tens of thousands of ADUs being permitted across the state. ADUs are often smaller attached or detached residential units that are secondary structures on a tract of land, and contain sufficient facilities for a resident to live independently.

On the other hand, Californians have been much less likely to use S.B. 9's authority to convert their homes or divide their lots. This authority had only been used 282 times about a year after the bill's passage, despite estimates that as many as 700,000 homes could be built under this new law.

In the past year, the Newsom administration and developers have started using existing legislative language to increase multi-unit dwelling construction more broadly, as well as counteract select localities' efforts to circumvent S.B. 9's requirements. A statute known as the "builder's remedy" lets developers go around local zoning codes in areas where local governments failed to lay out a plan for housing production to meet local needs. In these localities, developers can move forward with projects where either all of the units are priced at levels that are affordable for middle-income households, or at least 20% of the units are affordable for lower-income households. This has led developers in wealthy areas like Santa Monica and Beverly Hills to use the law's protection to apply for or initiate affordable housing projects that could have otherwise been blocked by local zoning rules.

Albuquerque, New Mexico: Increasing Supply through Building Conversions and ADU Construction

In July 2023, the city of Albuquerque adopted ADU and building conversion reforms. The changes will allow certain properties zoned for single-family home construction to build ADUs—also referred to as "casitas"—on their properties, which alone impacts up to 68% of all zoned properties in the city. Additionally, they provide for conversions of certain non-residential developments to multi-family unit dwellings, which can facilitate conversion of former hotels to residential units. The city has also considered other proposals to meet housing demand, which included eliminating maximum building heights, allowing single-detached homes to be converted to duplexes, and reducing parking requirements for multi-unit dwellings.

New Models for Financing Can Help Increase Affordable Housing Construction

Removing regulations alone will not solve the housing crisis.

While removal of zoning restrictions will help with the effort to increase the supply of housing, the market will not sufficiently increase the number of affordable housing units without additional government intervention. For example, developers may be drawn to developing in primarily higher-income areas, as they will be able to derive higher profits from units built on land with higher property values, and people will be willing to pay more to live in these neighborhoods.

Moreover, new buildings in lower-income areas could lead to unaffordable prices for current residents, who are likely living in older housing stock that is cheaper than newly-constructed housing. Absent any other policy changes, this could mean that new, wealthier residents would move into the new units, while lower-income renters would still face a housing shortage and the potential for displacement. Rising home values would also increase wealth for current homeowners, but renters could be harmed under these circumstances.

There is a growing recognition that governments need to do more to ensure that enough newly constructed housing is affordable to the lowest-income families. The Low-Income Housing Tax Credit (LIHTC) is a primary way that federal and state governments help finance new buildings with affordable rental units, but the program is oversubscribed and in need of reform to ensure it reaches those most in need. The bipartisan Affordable Housing Credit Improvement Act would increase the number of available credits to better meet demand while changing the program rules to make sure that more units were built to serve Tribal communities, rural areas, and other at-risk and underserved groups. State-level requirements for a minimum threshold of affordable housing per municipality, as is required in Massachusetts, could also be useful among other tools used to increase the number of affordable units. Without these mechanisms, prices for housing available to low-income families will likely remain elevated.

When coupled with zoning reform, changes to government funding mechanisms can help enhance lower-income families' access to housing in higher-income areas.

Reforms to government-financed affordable housing development programs can increase housing choice for low-income families. Historically, public housing investment has concentrated affordable housing in areas of high poverty, limiting low-income families' choice of where to live. More recent federal programs—aimed at reducing residential poverty concentration—then replaced low-income housing with mixed-income housing and led to low-income families' displacement. Some housing advocates also argue that LIHTC's current structure encourages low-income housing development primarily in low-income areas, forgoing an opportunity to provide lower-income families greater access to the economic and environmental advantages seen in higher-income areas. Housing vouchers enhance families' housing choice, and government efforts to supply affordable housing in areas of various income levels contributes to this end. While the following section discusses models for public financing of affordable housing stock, ensuring families' housing choice is key to equitable affordable housing development.

State and Local Models for Financing Increase Affordable Housing Stock

In recognition of the need for additional affordable housing supply, state and local governments are exploring financing incentives to increase the stock of housing that is affordable to low- and middle-income families without demand-side subsidies. Below are a few promising case studies for these efforts.

Maryland: Multiple Approaches to Affordability

The Housing Production Fund: Creating a Public Alternative to Private Housing Investment

In 2021, officials in Montgomery County, Maryland created a Housing Production Fund (HPF) to finance construction of mixed-income housing. The county's Housing Opportunities Commission (HOC) seeded the fund with $100 million in bond financing that the fund lends out to developers to help cover the costs of new construction. The HOC can compete with private investors because it can afford to receive lower returns from ownership shares in the property, as well as offer lower interest rates on loans, than what private equity firms or other investors would demand.

In exchange, the HOC requires developers entering into this agreement to set aside at least 20% of the new units for families earning at or below 50% Area Median Income (AMI), and at least 10% of the units for those earning up to 70% of AMI. This model allows private developers to make a profit, while the HOC retains an ownership stake that supports its goal of keeping people housed at affordable rates. Importantly, it can also maintain the pace of new construction when interest rates are high as they are now, by ensuring that developers can keep their financing costs down in exchange for creating affordable housing for more middle-class families. Developers recently completed one of the first projects that utilized the HPF: a 268-unit building, in which 25% of the units will be affordable to tenants with income levels at 50% AMI.

The Affordable Housing Opportunity Fund: Supporting Affordable Rent Levels for Tenants

In addition to the HPF, in 2022 the County created a $14 million Affordable Housing Opportunity Fund (AHOF) to make short-term loans to prospective building owners. The fund aims to support affordable housing developers in building purchases, to maintain affordable rents for existing affordable units. The short-term loans are meant to support rapid purchases of existing buildings that may otherwise be sold to landlords who could hike rents and make the units unaffordable.

New Mexico: Investing in Local Affordable Housing Trust Funds

Local governments across New Mexico have also been leading efforts to finance affordable housing stock. For example, in November of 2023, voters in Santa Fe approved a ballot measure instituting a tax on the sale of homes over $1 million, with proceeds directed to the city's Affordable Housing Trust Fund (AHTF), tasked with meeting the city's affordable housing needs. The tax—also referred to as the "Mansion Tax" would apply only to the value of a property above the $1 million threshold, at a rate of 3%. The city has estimated that the measure will generate approximately $6 million each year, providing the fund with a substantive dedicated revenue source. In 2022, voters in the City of Las Cruces also approved the issuance of a $6 million general obligation bond to fund its AHTF, which was established in 2010 and previously relied on limited capital infusions from the city's general funds. The city previously estimated that the initial $6 million investment could help leverage more than $36 million in funding from state, federal, and private sources, to create an additional 175 affordable housing units.

Maine: Enhancing Affordability in Rural Areas

Maine's Rural Affordable Housing Rental Program, launched in 2022 using $20 million in funds from the American Rescue Plan and MaineHousing bond issues, uses forgivable loans to incentivize affordable housing development in rural areas that might otherwise not draw new construction. Eligible applicants include public housing authorities, as well as nonprofit and for-profit developers, and the loans they receive can be forgiven for up to $185,000 per unit. The program targets rural areas for projects and is intended to help build 115 new units in rural Maine with existing funds. All units that benefit from the program must be leased to those making at or under 80% AMI, and any loan recipients must limit rent increases on supported units for the next 45 years. The program has already closed applications due to significant uptake, though Governor Janet Mills' recently passed FY 2024-2025 budget dedicated up to $35 million to the program to support continued operations.

The Biden Administration Is Taking Important Steps to Increase Housing Supply

Alongside the state and local efforts highlighted above, the Biden administration has advanced efforts to alter current land use laws and zoning regulations to ensure more Americans can afford a home that promotes their economic and social well-being. Specifically, the administration's Housing Supply Action Plan includes multiple programs that support housing construction. For example, the Pathways to Removing Obstacles to Housing (PRO Housing) program provides a total of $85 million in grants to localities that are taking steps to remove regulatory barriers for affordable housing construction. The FHA has also published a proposal to facilitate ADU financing and HUD has announced policy changes that will allow more, larger loans to qualify for the LIHTC program.

In addition, the American Rescue Plan's (ARP) State and Local Fiscal Recovery Funds (SLFRF) has helped to stimulate affordable housing construction and support housing stability. Between July 2022 and April 2023, state and local allocations towards housing construction, preservation and stability grew by 29%. The HOME program, which received $5 billion from the ARP to support affordable housing construction, rental assistance, and supportive housing services, is anticipated to increase affordable housing stock across the country by at least 20,000 units.

The administration is also working to support states and localities in office-to-residential conversion. It has created a $27 billion Greenhouse Gas Reduction Fund under the Inflation Reduction Act to, among other things, construct new buildings with zero emissions and support converting buildings from commercial to residential structures. Moreover, the administration has announced their plan to fund office-to-residential conversion research, as well as the creation of a guide implementing cost-effective conversion projects for states and localities.

Conclusion

States and localities across the country are working to reverse the consequences of existing zoning restrictions and provide more funding for affordable housing construction and maintenance. Congress can support these efforts by funding land use reform implementation, financing state and local efforts to build more affordable housing and investing more federal funds in new construction. The federal government is also well-positioned to help municipalities share information and ideas on the best ways to propose, pass, and implement zoning and land use reform. The federal government can also consider issuing a new example of legislative language that states and localities could use to undo the exclusionary models created in the 1920s and create more housing for all Americans.

No one program or policy will resolve the nation's housing crisis on its own. Coordination between state and local governments and the federal government can help ensure the array of policies aimed at increasing the supply of affordable housing for all Americans will be successful.