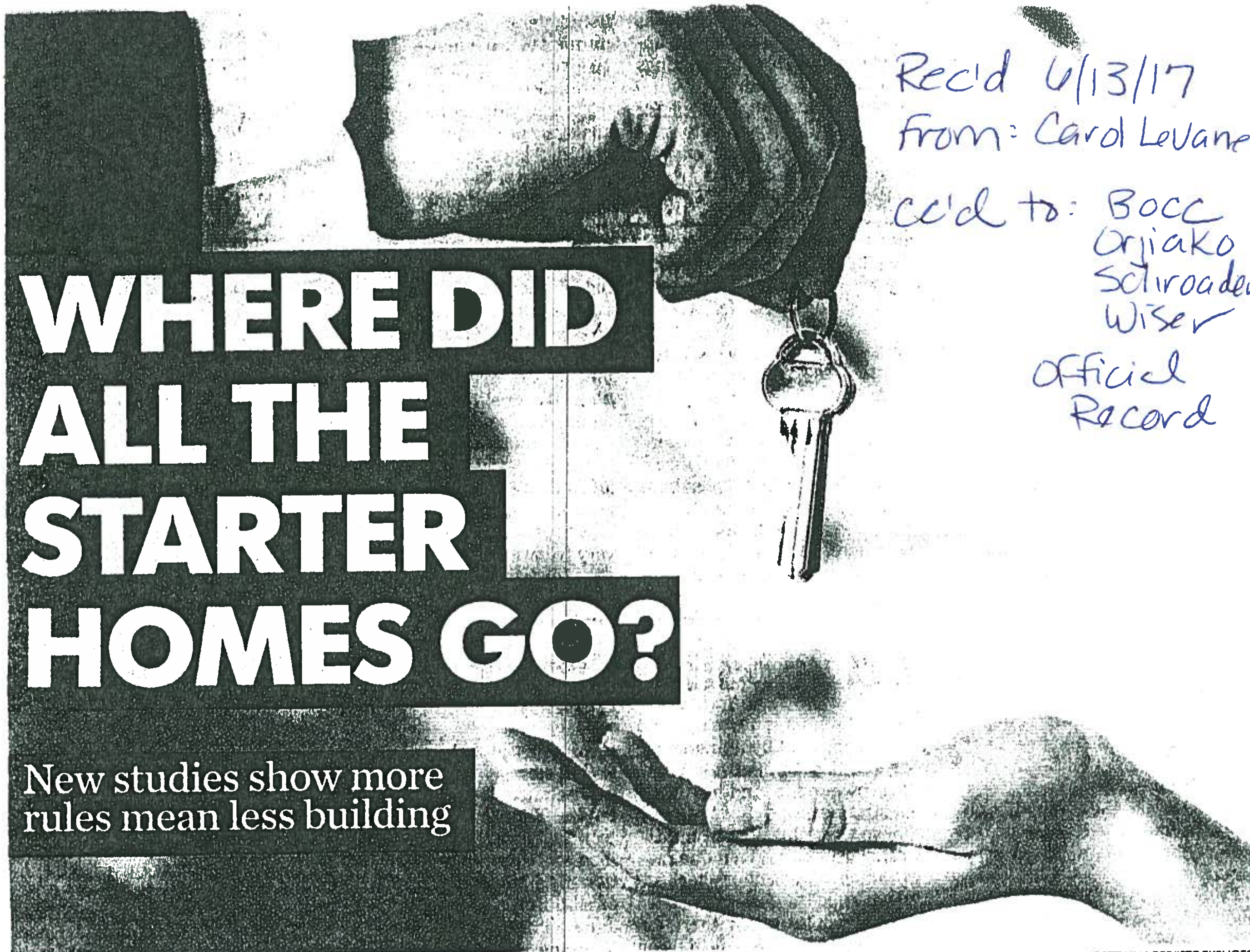
WHERE DID ALL THE STARTER HOMES GO?

New studies show more rules mean less building



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James and Carrie Finan have been house hunting in the Seattle area for four months in a seemingly futile race against time: They're living in a room in James' mother's house and their first child is due in September.

They've seen about 40 starter houses that match their criteria — $350,000 or less, three bedrooms, about 1,200 square feet — and made four offers ranging from $32,000 to $82,000 above asking price. They've lost out each time.

"Every time we hear we're not getting it, my heart kind of sinks," James, 29, says. "It's been insane."

A big reason the Finans are struggling is the regulatory morass faced by builders such as Mike Walsh. On a parcel in Sammamish, Wash., a Seattle suburb, he would like to build 36 relatively affordable houses. But since zoning changes in recent years permit just 25, he'll have to sell each at $1.2 million to make the project profitable.

An increasingly byzantine maze of zoning, environmental, safety and other requirements partly accounts for housing construction that remains 35% below normal levels across the country, especially for affordable starter houses, builders and economists say. And that building deficit is the chief culprit behind a skimpy supply of both new and existing homes that has driven up prices about 40% the past five years, says Lawrence Yun, chief economist of the National Association of Realtors. Rising prices are good for homeowners but shut out many buyers, such as Millennials shopping for their first house.

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There are other reasons single-family home construction is still sluggish: Builders are coping with shortages of lots and construction workers. And many banks have been reluctant to lend since the housing crash in the mid-2000s.

But while experts long have suspected that regulations were a deterrent for builders, new studies show more starkly that areas with the most rules — particularly big metro regions on the East and West coasts — have the least housing construction. Some of the rules aim to make homes safer or help neighborhoods deal with heavier rainfall and congestion.

A report by the National Association of Home Builders last year found that from 2011 to 2016, regulatory costs to build an average house had increased from about $65,000 to $85,000, or 30%, and continue to make up a quarter of the price of a home.

Jess Zimbabwe, who oversees land-use issues for the National League of Cities, an advocacy group for municipalities, argues regulatory costs make up a relatively small portion of rapidly rising home prices in big cities.

A new analysis of 189 metro areas by Federal Reserve economist Raven Molloy finds that, in the top third of most-regulated areas, 27% of owner-occupied homes are affordable to low- to

▶ STORY CONTINUES ON 2B

Rules slow housing starts

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moderate-income buyers. In the lowest third of least-regulated areas, 67% are affordable for that group. Regions with the most regulations and fewest starter homes include coastal cities such as Baltimore, Boston and Seattle as well as Denver and Phoenix. Areas in the South and Midwest have the fewest regulations and the most affordable units.

Expenses faced by developers and builders include applying for zoning approval; meeting environmental and energy-efficiency standards; water and sewage hookup fees; and the cost of delay as developers pay property taxes and interest on loans while land sits empty. Many cities have boosted minimum lot sizes and set aside more land for open space, which means fewer homes. They've also imposed rising "impact fees" on developers to defray the cost of widening roads to handle more traffic, for example.

Meanwhile, federal and state rules mandate that builders protect streams, ponds and wetlands, as well as a growing list of 1,447 endangered or threatened species that may reside on the property. Builders also must install ever more elaborate storm water retention facilities so as not to overwhelm sewers or pollute rivers.

Walsh, who owns Terrene Ventures, says that about a decade ago he routinely built a retention pond that would occupy three lots at a new housing complex in the Seattle area at a cost of $1,000 per house. Now, he must build a concrete "vault" that takes up eight to 10 lots and costs $10,000 to $15,000 per house.

Zimbabwe says the facilities are needed because climate change has intensified storms, and the spread of developed land increases water runoff.

It takes Walsh about nine months to get local, state and federal approvals for a development, up from three months 15 years ago, he says. Walsh, who builds 30 to 50 homes a year, figures he could put up perhaps twice as many if the time and costs to apply for the government blessings had not mushroomed.

Russell Hokanson, head of Seattle King County Realtors, a trade group, cites other reasons for the region's housing shortage, including its status as a technology hub and the third-best jobs engine in the country as of April.

But, he adds, "We are feeling the pinch now, and all the regulations that slow down (efforts) to get product into the market" are a big factor. The area has the country's fastest rising home prices.

Sammamish Mayor Don Gerend, says that since the early 2000s, the town has cut the number of homes permitted on a parcel of land, and impact fees have become the highest in the state.

"If we're going to have more growth here, it shouldn't be to the detriment of people who live here," Gerend says.

Faced with the higher costs, some builders simply abandon projects or put up pricier homes in order to maintain profit margins. A study of the Boston area in the Journal of Urban Economics concluded that each new rule reduces housing construction the following year by about 10%.

"There are a large number of ways to shut housing down, or to slow the process so that developers just give up," says Edward Glaeser, a Harvard University economist and co-author of the study. Glaeser has said existing homeowners, the constituents of municipal officials, generally oppose new developments.

Builders often respond by going ahead with a project but constructing pricier houses, as Walsh is doing, says Robert Dietz, chief economist of the National Association of Home Builders.

Some are undeterred. The ESG Companies has sought for nearly 30 years to put up 1,000 dwellings, including 500 starter houses, on a parcel in Chesapeake, Va. The state cleared the firm's plan to preserve wetlands, but the U.S. Army Corps of Engineers disagreed with the wetland delineation and asked it to consider other properties. After spending $20 million on surveys and other expenses, ESG is still awaiting approval of a scaled-down version of the complex. "It's very frustrating," ESG Vice President Michael Gelardi says.