

HOUSING AFFORDABILITY

State and local governments should

- reduce and eliminate zoning regulations and reduce permitting fees;
- establish an annual review of housing permitting and new construction figures to measure the effectiveness of state and local reforms; and
- overhaul local regulation to ensure fair and equal treatment of manufactured housing alongside traditional stick-built housing.

Congress should

- reform trade laws that lead to tariffs on key building inputs like lumber, cement, plywood, quartz, washing machines, wooden cabinets, and shelving units (for example, adding a "public interest" check prior to duties' implementation could prevent shortages of critical building materials);
- increase housing affordability and supply by making Tax Cut and Jobs Act reforms to mortgage interest and state and local tax deductions permanent and eliminating these deductions long term;
- revise depreciation schedules to allow for more rapid or immediate expensing of structures to encourage housing development;
- pass legislation so that federal lands that are not specially designated can be returned to state and local governments and used for new housing development;
- relax the definition of manufactured housing outlined in the National Manufactured Housing Construction and Safety Standards Act of 1974;
- eliminate the Department of Housing and Urban Development's "HUD Code," which unfairly targets manufactured housing for federal regulation; and

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- relax the Department of Energy's appliance and equipment standards to allow state and local governments to set their own standards.

The administration should

- eliminate Section 232 tariffs on steel and aluminum and Section 301 tariffs on Chinese imports via executive order to reduce the cost of construction materials and related products;
- abandon recent Department of Commerce policy changes that effectively ensure punitive duties on subject imports, including construction materials; and
- consider refraining from supporting projects for which the goal of efficient housing assistance is defeated by restrictive local regulation.

America has an acute housing imbalance. For many years, and in many places, housing supply has not met housing demand, and this has resulted in high and growing prices, especially in places like New York City, San Francisco, and Washington, DC.

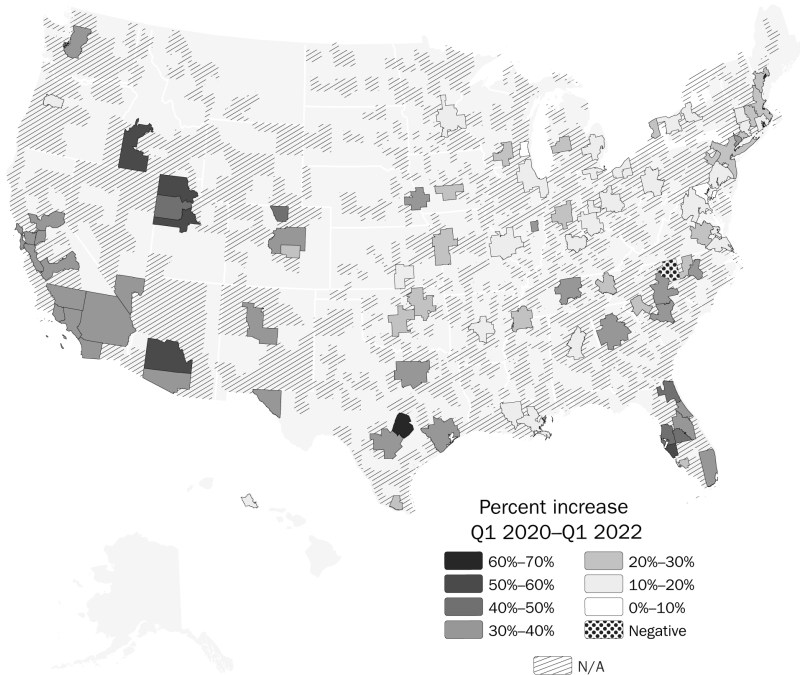
Housing supply challenges intensified during the COVID-19 pandemic. The number of “missing” housing units—or the number of units required to keep up with household formation minus existing units—grew from an estimated 2.8 million units in 2018 to 3.8 million units at the end of 2020. Housing inventory, another indicator of housing supply, plunged at the end of 2021 and was down more than 40 percent between December 2021 and the same month in 2019.

As housing inventory dwindled, prices rose (Figure 1). Prices for homes are up more than 20 percent from the beginning of the pandemic to the end of 2021, and rents are up over 15 percent during the same period. In markets with high levels of in-migration, including Florida and Sun Belt cities like Las Vegas, Miami, and Phoenix, price gains are even more extreme, with rents growing between 25 and 30 percent, year-over-year.

To improve housing affordability, it is necessary to build more housing. Escalating prices reflect a demand–supply mismatch resulting from a variety of factors, including substantial migration to Southern and Western cities, out-migration from central cities to surrounding areas, pandemic labor shortages, supply chain delays, and rising prices for construction materials like lumber and steel, all of which combine to limit the supply of new and existing homes.

Figure 1

During the pandemic, median home sales prices increased dramatically in many large U.S. metro areas



Source: “List and Sale Prices: Median Sales Price (Raw, All Homes, Monthly),” Zillow Research, <https://www.zillow.com/research/data/>.

Federal Policy Issues

Several of these factors, however, are exacerbated by preexisting federal policy. For example, tariffs have increased the cost of a wide variety of construction materials, including lumber, aluminum, and steel. These tariffs have worsened over time, and late in 2021, the U.S. Commerce Department increased duties on Canadian softwood lumber from 9 percent to 18 percent. Tariffs collected on carpets, flooring, countertops, and ceramic products have also increased in recent years. Recent economic analysis finds that U.S. tariff actions cause domestic construction material prices to increase significantly.

Federal tax deductions for property tax and mortgage interest also increase home prices, particularly in metropolitan areas with inelastic housing supply. These tax deductions make houses more valuable and increase people’s willingness to pay, thereby making it harder for first-time homebuyers to afford a down payment. Although the deductions were curtailed by the 2017 Tax Cut and Jobs Act (TCJA), under existing policy the TCJA limitations on itemized

deductions are set to expire, and a portion of both mortgage interest and state and local tax deductions remain.

Federal tax law affects housing in other ways. Current policy, for example, requires developers to write off the construction costs for new apartments over decades, which, because of inflation and the time value of money, raises the cost of development substantially. This feature of the tax code also has the unfortunate consequence of making non-real-estate investments with more favorable tax treatment more attractive than housing development, even when additional housing development is desperately needed. As a result, low-cost housing suffers as developers focus on luxury units, which have higher margins and can more easily absorb the additional cost.

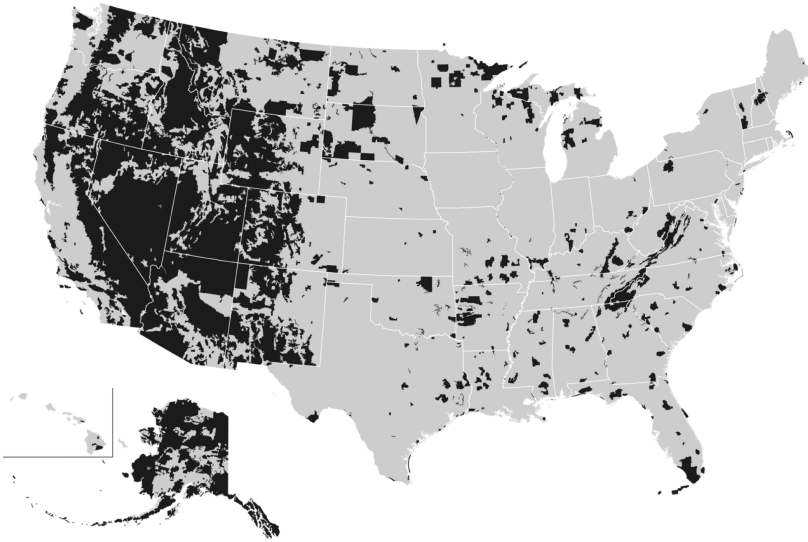
Federal policy also reduces the supply of land available for housing. In Western and Southwestern states with high in-migration, the federal government owns a large amount of state land (see Figure 2), making it unavailable for development of any kind, including housing development. For example, in Nevada, Utah, and Idaho, the federal government respectively owns 80 percent, 63 percent, and 60 percent of the land. In other states, including Montana, New Mexico, Oregon, and Wyoming, the federal government owns about half to one-third of available land.

In fast-growing states, these federal lands frequently touch urban or suburban areas—thus acting as a hard barrier to the localities' expansion. For example, the real estate intelligence platform Geomancer estimates that 217,000 acres of U.S. Forest Service (USFS) and Bureau of Land Management (BLM) lands are *within* Utah city boundaries, and 650,000 acres of USFS and BLM lands are within one mile of city borders. As demand for housing increases in areas bordering—and thus constrained by—federal lands, prices are sure to rise.

Finally, federal policy and industry lobbyists have worked overtime to put low-cost manufactured housing at a disadvantage. Specifically, the provision of low-rate Section 235 mortgage loans for traditional stick-built homes only and the regulation of typically cheaper manufactured homes through the Department of Housing and Urban Development's Manufactured Home Construction and Safety Standards—more commonly known as the HUD Code or national building code—have made it more difficult for manufactured housing to compete with their stick-built counterparts. Although the Section 235 program is now obsolete, HUD still requires manufactured housing to be attached to a chassis, or metal base frame (typically of a motor vehicle), which allows local governments to regulate manufactured homes more restrictively, as if they were mobile homes. Such restrictions deny American workers more affordable manufactured housing options.

Figure 2

The federal government owns large amounts of land in Western states with high in-migration



Source: "USA Federal Lands," ArcGIS Living Atlas of the World, updated May 23, 2022.

Other federal laws and regulations, such as the Department of Energy's appliance and equipment efficiency standards, presumably also raise the cost of housing.

State and Local Policy Issues

Arguably more important than any policy at the federal level, however, are ever-increasing state and local regulatory constraints: ultimately, the way to improve housing affordability is to allow people to build housing. Unfortunately, land-use regulation continues to limit housing supply by increasing development costs, creating uncertainty, and producing delays. These regulations determine everything from the height, width, and architectural features to the use of a given property, and they subject development to lengthy review processes with many veto points. Together, zoning regulations effectively freeze preexisting development patterns, which makes it difficult to grow or accommodate new residents.

Scores of research papers tie land-use regulations to increased housing prices. One study found, for example, that zoning regulations pushed up the cost of apartments by about 50 percent in Manhattan, New York, and San Francisco

and San Jose, California. This figure has likely only grown as regulatory constraints and demand have increased in recent years.

In addition to increasing regulatory obstacles, developer impact fees have grown over time. One survey found that the fees had grown by 45 percent between 2005 and 2016 to an average of \$21,000. These fees land hard on starter homes, where would-be tenants are less able to absorb the costs.

Meanwhile, local building codes—which include structural, plumbing, mechanical, electrical, accessibility, and energy-related requirements—also raise the cost of housing. Although their original purpose was to protect public health and safety, building codes have strayed from that goal and are used to achieve other objectives, like increasing perceived housing quality or pursuing environmental goals, with costly consequences. For example, stricter state building energy codes aimed at reducing energy-related environmental externalities have been observed to reduce the number of bedrooms and square footage of homes at the lowest end of the income distribution.

These policies and others that restrict housing development are important to Americans for many reasons, including that housing availability and affordability continue to influence employment opportunities for the roughly three-quarters of workers who work onsite full- or part-time. In the past, research found that less skilled workers could not afford the higher housing costs in heavily regulated cities with strong economic opportunities, and so these workers became stuck in lower-cost areas that have fewer job opportunities. Although remote work is changing the geography of work opportunities for some workers, it seems unavoidable that housing will continue to function as a *de facto* gateway to vital economic, educational, and social opportunities for many years to come.

Policy Recommendations

Although migration patterns, supply chain delays, and inflation will continue to put pressure on U.S. housing prices, smart policy reforms can serve as an essential release valve. Policymakers should pursue market-oriented reforms that will increase residential construction and lower housing prices for all Americans.

At the federal level, trade policy should be reformed to reduce the cost of housing materials. Although U.S. antidumping and countervailing duties are difficult to eliminate, the administration should work with Congress to reform the process that led to these tariffs in the first place (e.g., by allowing administering agencies to consider the consumer and broader economic harms of proposed duties). The administration also can and should unilaterally eliminate Section 232 tariffs on steel and aluminum imports, as well as Section 301 tariffs

on Chinese imports of various building materials and appliances. And the administration should relax or eliminate federal appliance and equipment efficiency standards that add to the expense of housing.

Congress can also play an important role in improving housing supply and affordability. For example, Congress should make permanent the limits that the TCJA placed on state and local tax deductions and the mortgage interest deduction and should in the long term work to eliminate these deductions. To encourage housing development, Congress should reform the tax treatment for development by allowing more rapid, ideally immediate, expensing of structures. According to Tax Foundation estimates, a more neutral tax approach would reduce construction costs by about 11 percent, which would make low-income units both more affordable and more likely to be built.

Congress should also increase the amount of land available for housing and development in Western and Southwestern states that are experiencing high levels of in-migration. To that end, Congress could pass a law that requires the federal government to return some of the 640 million acres of federally owned land to state and local governments or private owners. Such a law could apply to lands that are not specially designated or sensitive (lands that are not national monuments, critical areas, national recreation areas, etc.).

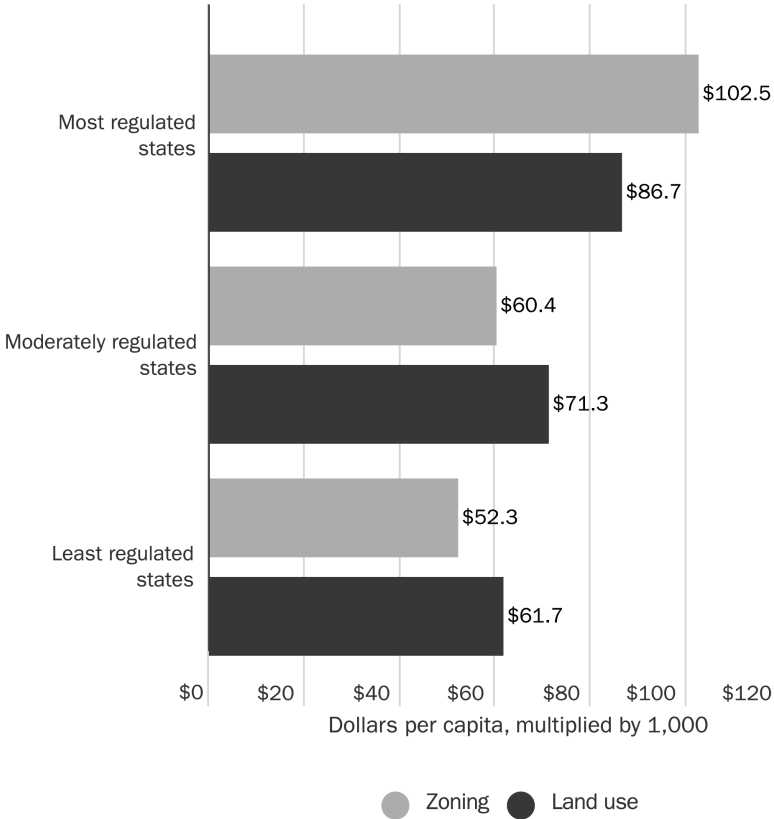
The Southern Nevada Public Land Management Act (SNPLMA) is an example of an existing program that returns federal land to private hands, and this program could be used as a template. The program makes federal public land in Clark County, Nevada, available for auction. Under the SNPLMA, the revenue resulting from the sale of federal lands is returned to the secretary of the interior to be used for environmental conservation and projects, to the state of Nevada to be used for educational purposes, and to the Southern Nevada Water Authority. As a result, many interested stakeholders benefit from the sale of federal public lands.

A new bill with objectives similar to the SNPLMA but with more of a focus on housing development—the Helping Open Underutilized Space to Ensure Shelter Act (HOUSES Act)—was introduced earlier this year. This bill or something like it could increase the amount of developable land in Western states.

Although zoning reform is mostly a state and local issue, some policymakers and analysts have suggested federal reforms to encourage states and localities to deregulate more comprehensively. For example, federal housing subsidies are concentrated in the most restrictively regulated states (see Figure 3), which means that states and cities that actively create housing affordability issues via restrictive zoning practices are rewarded for doing so.

Figure 3

Federal housing affordability subsidies are largest in the most regulated states



Source: Vanessa Brown Calder, “Zoning, Land-Use Planning, and Housing Affordability,” Cato Institute Policy Analysis no. 823, October 18, 2017.

Unfortunately, current federal programs provide incentives for state and local governments to ignore local contributions to the housing affordability crisis. Federal money cannot adequately compensate for the effect of local zoning and land-use regulations on housing affordability (and even if it could, using federal funds to back damaging local policy is wasteful).

To align incentives, housing affordability programs should ideally be funded and administered by state and local governments. In the meantime, federal agencies should consider refraining from supporting projects for which the goal of efficient housing assistance is defeated by restrictive local regulation.

Finally, governments should remove disparate regulatory burdens on manufactured housing. In its Housing Supply Action Plan, the Biden administration indicates its intent to update the HUD Code regulating manufactured housing “to allow manufacturers to modernize and expand their production lines,”

among other reforms. This proposal appears well-intentioned, but its scope and timing are unclear. Congress should take action to eliminate the requirements mandating that manufactured housing be attached to an unnecessary, permanent chassis, as well as HUD’s national building code, which unfairly targets and regulates manufactured housing. Meanwhile, local governments should review and overhaul relevant regulations to ensure that manufactured housing is treated the same as other housing types.

At the state and local level, policymakers must continue to find ways to relax zoning and building requirements and reduce permitting costs. In recent years, some states and cities—such as California, Connecticut, and Minneapolis, Minnesota—have upzoned areas from low to moderate density, relaxed regulations like parking requirements, and legalized accessory dwelling units (colloquially “granny flats”) to increase housing supply and reduce costs. Unfortunately, these changes often exist within the context of broader restrictions on building height and size that make increasing density unprofitable; additional regulatory and process reforms are needed.

Conclusion

Government policy has contributed to high and rising home prices in numerous ways. Fortunately, federal, state, and local officials could do much to improve housing affordability. To moderate future home price increases and improve economic opportunity for all workers, governments at all levels should reform policy to lower construction costs, increase housing supply, and correct demand distortions.

Suggested Readings

- Barattieri, Alessandro, and Matteo Cacciatore. “American Protectionism and Construction Materials Costs.” Cato Institute Briefing Paper no. 133, February 9, 2022.
- Calder, Vanessa Brown. “Zoning, Land-Use Planning, and Housing Affordability.” Cato Institute Policy Analysis no. 823, October 18, 2017.
- Elmendorf, Chris. “Recalibrating Local Politics to Increase the Supply of Housing.” *Regulation* 42, no.2, Summer 2019, pp. 38–55.
- Gray, M. Nolan. *Arbitrary Lines: How Zoning Broke the American City and How to Fix It*. Washington: Island Press, 2022.
- Kendall, Ross, and Peter Tulip. “The Effect of Zoning on Housing Prices.” Cato Institute Research Briefs in Economic Policy no. 124, August 1, 2018.

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