Testimony of Steven E. Lawson

On Behalf of the

National Association of Home Builders

Before the

House Financial Services Committee

Subcommittee on Housing and

Insurance

Hearing on

“The Cost of Regulation on Affordable Multifamily Development”

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Introduction

Chairman Duffy, Ranking Member Cleaver and members of the subcommittee, I am pleased to appear before you today on behalf of the National Association of Home Builders (NAHB) to discuss the impact of regulatory burdens on multifamily housing developments.

My name is Steve Lawson. I am a third-generation home builder from Virginia. As president of The Lawson Companies, I oversee a portfolio of more than 5,000 apartments and $15 million in annual construction and development. I also serve as chairman of NAHB's Multifamily Council, which represents NAHB members who build market-rate and affordable rental apartment buildings, condominiums for sale, student rental housing and mixed-use development projects.

NAHB represents more than 140,000 members who are involved in building single-family and multifamily housing, remodeling and other aspects of residential and light commercial construction. NAHB's members construct approximately 80 percent of all new housing in the United States each year. Many of our builders, including myself, rely on federal programs to help provide decent, safe and affordable multifamily housing to millions of our fellow Americans.

I would like to thank the subcommittee for holding this important hearing. Reasonable people would agree that there is a role for sensible regulations to protect health, safety and fair housing rights. Today we have the opportunity to examine the impact on affordable housing when regulations at all levels of government exceed these traditional parameters and the regulatory process becomes a vehicle to advance other public policy goals. At a time when affordable housing is out of reach for so many Americans, and new estimates from NAHB and the National Multifamily Housing Council (NMHC) indicate regulatory costs account for nearly one-third of the cost of multifamily development, it is not hard to conclude that overregulation is stifling new production of rental housing.

My testimony will emphasize the following themes:

- NAHB's economic forecast for multifamily production indicates demand remains strong, but production is constrained by regulatory burdens, high cost of building materials and labor shortages;
- A new joint study by NAHB and NMHC, estimates that regulations account for 32 percent of the cost of multifamily development. Therefore, NAHB recommends that policy makers:
  - Consider the *cumulative* effects of regulatory requirements to determine whether a new mandate is necessary to protect the health and safety of the public, or if it is simply a means to achieve a policy goal;
  - Remove barriers to production of multifamily housing;
  - Ensure that energy codes and standards are cost-effective, affordable and have a reasonable payback period of 10 years; and
  - Common sense updates to Davis-Bacon wage determination policies would help builders construct more affordable housing;
- Fair housing laws are important, and NAHB sees an opportunity to make constructive improvements to the Affirmatively Furthering Fair Housing (AFFH) Rule;
- The Trump Administration must resolve issues related to lumber and steel tariffs, which have needlessly raised the price of building materials;
- Multifamily builders and developers need reliable access to credit; and

- It is essential to maintain and properly fund federal rental assistance and multifamily production programs to serve very-low-income and extremely low-income Americans

Economic Data on Multifamily Housing

The demand for multifamily housing is still strong, but builders' confidence in the market has taken a slight hit recently.

Multifamily Production

From 1997 to 2006, a period seen as normal, multifamily housing starts averaged 340,000 units annually. Production fell to a low of fewer than 120,000 units per year in 2009 and 2010. Though annual production levels have recovered, they still have not been able to compensate for the severe lows in 2009 and 2010.

NAHB's most recent housing forecast calls for 376,000 multifamily housing starts in 2018 and an average of 355,000 starts from 2018 through 2020. These projections equate to multifamily housing starts of about 11 percent above the normal rate of 340,000 in 2018 and an average of about 4.5 percent above the normal rate from 2018 through 2020. Considering there are more than 135 million housing units in the U.S., multifamily housing units are contributing less than three-tenths of one percent to the housing stock per year.

In 2006, prior to the downturn, the homeownership rate was nearly 69 percent. Today, the homeownership rate is slightly over 64 percent. In the decade from the first quarter of 2007 through the first quarter of 2017, year-over-year growth in renter households averaged roughly 860,000 households. Although the number of renter households has declined slightly since the start of 2018, as the homeownership rate has recovered somewhat, it is still clear that the growth in the number of renter households has far exceeded the number of multifamily housing units being built. Additionally, the new construction of multifamily housing units that has taken place has served the upper end of the market.

Moreover, renters typically have more modest incomes. The latest available data from the American Community Survey show that median income of renter households in 2016 was $37,264. To be considered affordable, according to the conventional criterion, housing costs for a household at this income level should be no more than about $930 per month, or 30 percent of income. However, in the same year, the median asking rent for apartment units completed (in buildings with at least 5 apartments) was almost $2,200. This amount did not include any utility costs in cases where they are paid directly by the tenant. Only 11 percent of the apartments completed in 2016 had asking rents under $1,050—which is still above the level that would make them affordable to the median renter.

The reason such a large segment of the rental market is not being served by new multifamily construction is not because developers are unwilling to build for this market segment. Most often it is because those developers' costs of acquiring the land and building on it are too high to allow them to do so unless they receive a substantial government subsidy.

A significant category of these costs is the cost of local, state and federal regulation that a developer faces.

Multifamily Production Index and Multifamily Vacancy Index[1]

NAHB monitors multifamily builder and developer confidence in the market through its Multifamily Production Index (MPI). The MPI measures builder and developer sentiment about current conditions in the apartment and condo market on a scale of 0 to 100. The index and all of its components are scaled so that a number above 50 indicates that more respondents report conditions are improving than report conditions are getting worse. In the second quarter of 2018, the MPI showed that confidence slipped two points to 51, compared to the previous quarter. Although the MPI dropped slightly compared to the first quarter of 2018, an MPI above 50 still reflects a solid number of multifamily starts this year.

The MPI is a weighted average of three key elements of the multifamily housing market:

- Construction of low-rent units—apartments that are supported by low-income tax credits or other government subsidy programs;
- Construction of market-rate rental units—apartments that are built to be rented at the price the market will hold; and
- Construction of for-sale units—condominiums.

The component measuring low-rent units rose three points to 57, while the component measuring market rate rental units fell six points to 50 and the component measuring for-sale units dropped three points to 46.

NAHB's Multifamily Vacancy Index (MVI), which measures the multifamily housing industry's perception of vacancies, rose three points to 45 in the second quarter of 2018. The MVI is a weighted average of current occupancy indexes for class A, B, and C multifamily units, and can vary from 0 to 100, where any number over 50 indicates more property managers report more vacant apartments. Although the MVI increased in the second quarter, a reading of 45 is still seen as a healthy number for the multifamily market.

Multifamily builders and developers are seeing strong demand, but there are headwinds that have impacted further development. Some developers have had difficulty getting projects off the ground due to regulatory burdens and neighborhood opposition in certain parts of the country. In addition to regulatory costs, developers still need to monitor the impact of tariffs and the threat of further trade restrictions on building materials prices, especially lumber.

Regulations Account for Nearly One-Third of the Cost to Develop Multifamily Housing

Home builders and their subcontractors are among the small businesses that are disproportionately burdened by complicated regulations and expensive compliance costs. The multifamily sector is particularly subjected to these obligations. Overregulation of the housing industry is felt at every phase of the building process. It results from local, state and federal mandates. It includes the costs of applying for zoning and subdivision approval, environmental mitigation, and permit, hook-up, impact and other government fees paid by the builder.

These added costs result in higher rents and reduced affordability. In many cases, these projects become financially infeasible and, therefore, not built. Multifamily developers cannot

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[1] Please see "Multifamily Market Survey Second Quarter 2018" National Association of Home Builders Economics and Policy Group, August 23, 2018.

secure financing unless they can demonstrate to lenders that the rents will be sufficient to cover costs and pay off the loans.

As a small business owner operating in a heavily regulated industry, I understand how difficult (and often costly) it can be to comply with the myriad of government regulations that apply to my day-to-day work. This is particularly noteworthy in an industry where margins are so thin and consumers' sensitivity to price fluctuation is so acute.

According to *Multifamily Cost of Regulation*, a study conducted jointly by NAHB and NMHC, regulation imposed by all levels of government (whether local, state or federal) accounts for 32.1 percent of the cost of an average multifamily development. This study is based primarily on a survey of multifamily developers from both organizations.

Before I discuss the results of this analysis, I would emphasize that NAHB does not believe ***all*** regulation is bad. However, mandates at all levels of government have expanded beyond basic safety and soundness considerations and morphed into complicated compliance regimes, expensive code changes, energy efficiency mandates and/or restrictive land use policies. The compliance costs and fees associated with such policies are exacerbating the difficulty of providing safe, decent, and affordable rental housing.

When regulatory and compliance costs account for nearly one-third of the project cost, or exceed 42 percent in some cases, it is time to take a hard look at the *cumulative* effect of regulatory requirements. It has become relatively common for proposed federal legislation or regulations to encourage local jurisdictions to adopt particular types of building codes or land development patterns. An informed discussion of these proposals should recognize that, on average, regulation already accounts for almost one-third of a new multifamily project's development and building costs.

Multifamily Cost of Regulation Joint Study

The purpose of the joint analysis is to raise awareness of how much regulation currently exists, how much it costs and to encourage governments to do a thorough job of considering the implications for housing affordability when proposing and implementing new directives.

The only way to gather comprehensive data is by questioning multifamily developers, as they are the only ones who experience the wide range of forms regulation can take. NAHB and NMHC set out to accomplish this through a survey of both memberships. The purpose of the survey was to quantify how much regulation exists and how much it is adding to the cost of developing new multifamily properties.

Since multifamily developers do not, in general, have accounting systems designed to tease out these regulatory costs, NAHB and NMHC crafted questions for developers about the typical projects they build, including delays and costs incurred at different stages of the development process. Developers were asked to provide all hard costs as a percent of total development costs for their typical projects.

Housing affordability is a serious issue throughout the country, and this new research only further illustrates how the layers of excessive regulation translate into higher rents and reduced affordability for consumers. The results show that well over 90 percent of multifamily developers typically incur hard costs of fees paid to local governments, both when applying for zoning

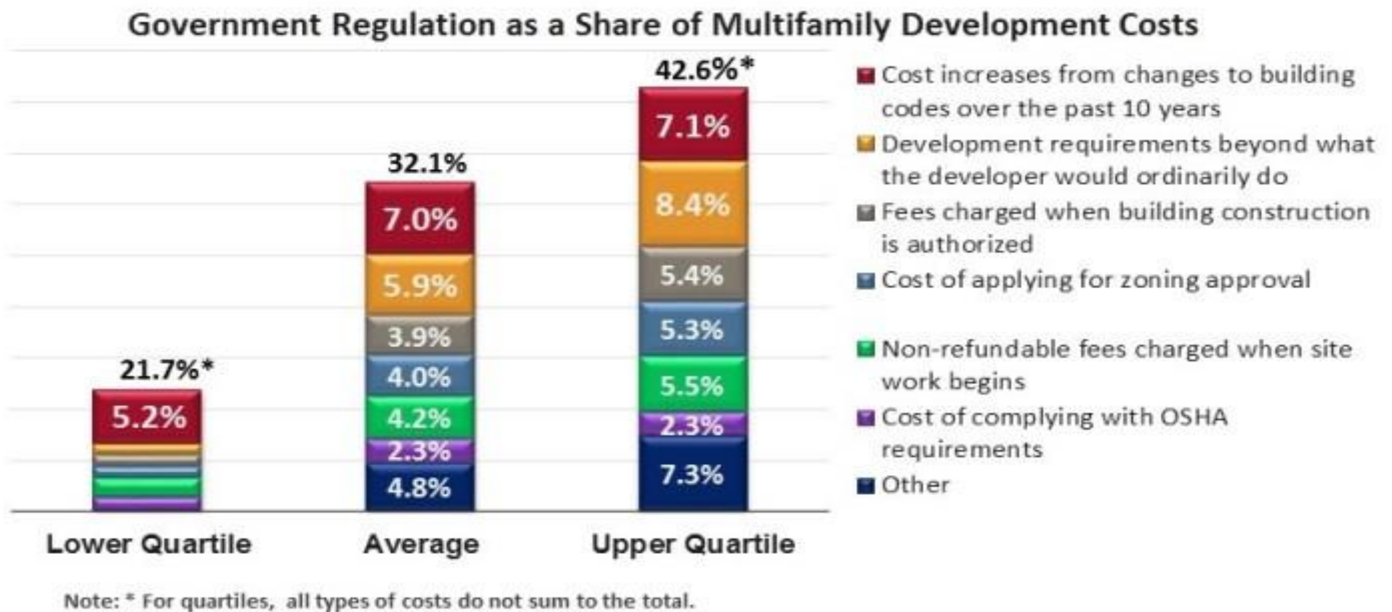
approval, and again when local jurisdictions authorize the construction of buildings. The study also shows that government regulations often imposes costs in other ways. Although local governments generally have authority for approving development and adopting building codes, state and federal governments are increasingly becoming involved in the process and layering on additional levels of fees and regulations.

The components that have the biggest cost impact are changes to building codes and costs attributable to development requirements (such as streets, sidewalks, parking, landscaping and architectural design) that go beyond what the developer would ordinarily provide.

Changes to building codes over the past 10 years have accounted, on average, for 7.0 percent of the cost of developing the property. No one would argue against standards for basic soundness and safety of structures, but building codes have expanded well beyond this.

The requirements by many local governments for new development to conform to community design standards (for example, streets, sidewalks, parking, height of buildings, landscaping, and architectural design) impose added costs if these standards go beyond what a multifamily developer would normally provide. These beyond-ordinary development requirements were the second most costly type of regulation, accounting for 5.9 percent of development costs, on average.

The chart below shows the average costs for the various types of regulation covered in the NAHB-NMHC study.



In the chart, the “other” category includes interest on refundable fees charged when site work begins, the value of land that the developer must dedicate to the government or otherwise leave unbuilt, the cost of so-called affordability mandates imposed without any incentives to offset the cost, and a “pure” cost of delay (i.e., how much the delay would cost even if regulation imposed no other type of cost).

As mentioned above, on average these costs add up to 32.1 percent of the cost of developing a new multifamily property. One-fourth of the time they reach as high as 42.6 percent. Oftentimes, these regulations end up pushing the prices of housing beyond the means of many middle-class working American families. The extent of the impact varies widely across states and metro areas, depending on population, income distributions and new home prices. This highlights the real effect that building regulations have on housing affordability.

Although local governments generally have authority for approving development and adopting building codes, state and federal governments are becoming increasingly involved in the process. Sometimes the federal government involvement is readily apparent, as when issuing storm water permits or enforcing OSHA requirements. Other times, the federal government involvement is less obvious. Examples include federal participation in the development of model building codes, and attempts to influence local development through conditions for obtaining grants or other sources of funding. Sometimes, indirect influences like these make it impossible to untangle which level of government is ultimately responsible for a given dollar of regulatory cost.

The current estimate that government regulation accounts for 32.1 percent of total development costs is almost certainly understated. It was not possible to account for items like the effects of tariffs on building materials or the extent to which local jurisdictions may empower their citizens to oppose multifamily housing in their communities. Average costs could be even higher now or in the near future due to regulations taking effect since the multifamily projects in the survey were completed. For example, OSHA's Silica Rule went into effect in late 2017, a regulation that industry groups have criticized as unreasonably onerous and unnecessarily costly. Similarly, local jurisdictions are just beginning to adopt the 2018 versions of the model international building codes which are estimated[2] to add thousands of dollars to the cost of a multifamily building. Several of these cost-increasing changes were supported by federal agencies.

Specific Burdensome Regulations

Building Codes

Virtually no one would argue against public standards for basic soundness and safety building codes for residential structures. Over the decades, however, building codes have expanded well beyond the basics. They are increasingly used as a vehicle to advance various policy objectives. In particular, federal agencies, such as the Environmental Protection Agency (EPA), the Federal Emergency Management Agency (FEMA) and the Department of Energy (DOE) actively participate in the development of national model codes, proposing changes to national model codes and testifying in favor of them during code hearings

As previously noted, the highest regulatory costs identified in the NAHB-NMHC study were changes to building codes over the past 10 years. These code changes accounted for an average of 7.0 percent of property development costs.

[2] Home Innovation Research Labs. "Estimated Costs of the 2018 ICC Code Changes for Multifamily Buildings," April 2018.

Moreover, the costs associated with building codes are still on the rise. A report by the Home Innovation Research Labs[3], *Estimated Costs of the 2018 ICC Code Changes for Multifamily Buildings*, shows minimum cost impacts for typical multifamily buildings ranging from $2,500 for a small 2-story multifamily project to $25,000 for a larger 5-story project.

The higher costs are primarily due to significant changes involving elevators and wind load design.

Home Innovation looked at four multifamily buildings ranging from a 2-story, 24-unit building to a 5-story, 167-unit building. Two of the four buildings included public spaces such as community or fitness rooms, leasing offices or retail spaces. The study also looked at a typical 4-story townhouse. All the buildings were selected from actual completed projects certified by Home Innovation under the ICC-700 National Green Building Standard.

The 2018 International Building Code (IBC) requires all elevators, including service elevators and elevators not accessible to the public, to have a two-way text-and video-based communication system for the hearing- and speech-impaired. It was difficult to quantify the cost, as no consensus standard for such a system exists, but an estimated cost per elevator is between $2,500 and $5,000. While proposed by a private individual, inclusion of this system was supported by the Department of Housing and Urban Development (HUD) and the US Access Board, despite it not being a requirement of the Fair Housing Act or the ADA, or otherwise included in nationally-recognized, consensus-based accessibility standards.

Revisions to design methods for wind resistance in the 2016 edition of the ASCE 7 Minimum Design Loads for Buildings and Other Structures standard, incorporated by reference in the 2018 IBC, significantly increased costs for roof construction..

Cost increases of $2,400 to $4,300 per building were estimated for buildings with steep-sloped hip- or gable-roofs, commonly seen in suburban condominium or apartment complexes. Buildings with low-slope roofs, more commonly seen in dense, urban environments, could see cost increases of $8,400 to $16,700 per building.

Fire code officials' ability to require a fire watch during construction was strengthened and expanded in response to a perceived increase in such fires. For larger projects, the cost to provide a 24/7 fire watch can exceed $233,000. Industry coalitions are working to address this issue by educating contractors regarding fire-safe work practices and do not believe increased and burdensome regulations are necessary.

Energy Efficiency

A leading example of how codes are used to advance policy objectives is energy efficiency. For instance, DOE has a share of its budget set aside for persuading state and local jurisdictions to adopt more stringent codes to promote energy efficiency objectives. Representatives from NAHB who witnessed all of the recent code hearings have criticized federal agencies for supporting certain code changes that removed flexibility and limited builders' options, driving up costs without improving energy efficiency, and to the benefit of specific product manufacturers.

[3] Home Innovation Research Labs is an independent subsidiary of NAHB.

NAHB agrees that energy efficiency is a worthwhile objective, and we support a number of voluntary initiatives and research to promote this goal. Nevertheless, up-front costs of these initiatives must be kept within reasonable bounds. NAHB strongly urges that energy codes or standards must be cost-effective, affordable, and supported by a reasonable payback period of 10 years.

Implementation of Davis-Bacon and Related Acts

Davis-Bacon prevailing wage requirements apply to a number of HUD's programs, including Federal Housing Administration (FHA) multifamily mortgage insurance programs for new construction and substantial rehabilitation. These critical mortgage insurance programs, especially HUD's Section 221(d)(4) program[4], enable NAHB's members to develop apartment communities affordable to low-and-moderate-income families. For multifamily builders, the requirement to use Davis-Bacon wage rates artificially drives up the cost of constructing affordable housing. NAHB is concerned that these policies will dissuade builders and lenders from using FHA multifamily mortgage insurance programs, resulting in fewer affordable units for hard working Americans during an affordable housing crisis. Further, the compliance burdens are creating barriers to entry for small mom-and-pop subcontractors to work on these projects.

Several key steps in the wage determination process can be improved, but achieving such results will require an ongoing commitment from the senior leadership of both HUD and the U.S. Department of Labor (DOL). Two of the most important Davis-Bacon policy issues that require inter-agency cooperation are resolution of split wage determinations on residential buildings and improving the timing for assignment of wage rate determinations.

Davis-Bacon Split Wage Determinations

Under Davis-Bacon, there are four basic categories of wage determinations based on the type of construction: residential (projects with no more than four stories), building, heavy and highway. DOL and HUD guidance set a threshold for determining substantial construction which requires a separate wage determination, and incidental construction which does not.

Using its 1996 Labor Relations Letter No. LR-96-03[5], HUD would issue one Davis-Bacon wage determination for multifamily properties if construction items (such as parking, club houses, streets etc.) are incidental in function to the overall character of the project, and if there is not a substantial amount of construction in the other categories. Except in the most extraordinary circumstances, the residential classification would not be altered by the cost of incidental items, even if their costs reached the "substantial" thresholds. "Substantial" construction is defined under various handbooks and guidance documents as greater than 20 percent of total project cost and/or $1 million or more in terms of absolute cost. Multiple wage determinations *could* be required when a project included separate and distinguishable

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[4] HUD's Section 221(d)(4) program insures mortgage loans to facilitate the new construction or substantial rehabilitation of multifamily rental or cooperative housing for moderate-income families, elderly, and the handicapped. It is the largest of the FHA multifamily mortgage insurance programs for new construction and substantial rehabilitation.

[5] HUD (OLSE) Labor Relations Letter No. LR-96-03 "Application of Department of Labor guidance concerning 'projects of a similar character'" to Guide Davis-Bacon Wage Determination Policies (12/02/1996)

components that fall into different construction categories and the components are not incidental to each other, but multiple wage determinations on HUD multifamily jobs were extremely rare.

In 2013, DOL directed HUD to revise its Davis-Bacon guidance documents and handbooks. DOL objected to FHA's broad interpretation of incidental construction, and directed HUD to scrutinize the cost of construction items that exceed 20 percent of the total project cost or cost more than $1 million.

Unfortunately, the policies DOL directed HUD to use for assigning split Davis-Bacon wage determinations to "substantial construction"[6] items on residential apartment projects are jeopardizing FHA-insured multifamily deals. Since 2016, it has become common for multifamily lenders and borrowers seeking FHA mortgage insurance to be assigned split wage decisions for residential properties when construction items exceed $1 million in costs, even though the items historically have been treated as incidental construction.

The $1 million threshold is especially problematic for multifamily properties. On larger projects, it is not difficult for the cost of garages, club houses, landscaping, roads and other common apartment components to exceed this threshold. As the cost of construction continues to climb, this figure will be even more easily surpassed. DOL's insistence that HUD use the $1 million cost threshold as a basis for assigning separate wage determinations results in confusing, costly and administratively burdensome split wage decisions on residential projects. In many cases, borrowers and lenders receive this information very close to the closing date on their loans, and must substantially re-work the deals at the last minute to make them feasible.

For these reasons, NAHB requested DOL and HUD to enact policies that account for the current realities of residential construction. NAHB continues to strongly encourage DOL to draft a wage determination policy with HUD that:

- Classifies any housing development project that is 4 stories or less as "residential;" and
- Does not alter the residential classification by assigning a split wage determination based on the cost of construction for items, unless those costs exceed 20 percent of total project costs.

Alternatively, DOL and HUD could simply reaffirm Labor Relations Letter No. LR-96-03 as the appropriate guidance for FHA insured residential projects.

<u>Timing of Davis-Bacon Wage Rate Determinations</u>

When borrowers use FHA multifamily mortgage insurance for new construction or substantial rehabilitation, unexpected changes in Davis-Bacon wage rates that occur late in the application process may result in higher rents to tenants or even totally derail a project.

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[6]DOL is relying on these documents: U.S. Department of Labor Employment Standards Administration Wage and Hour Division All Agency Memorandum No. 130 "Application of the Standard of Comparison 'Projects of a Character Similar' Under The Davis-Bacon And Related Acts" (3/17/1978) and U.S. Department of Labor Employment Standards Administration Wage and Hour Division All Agency Memorandum No. 131 "Clarification of All Agency Memorandum No. 130" (7/14/1978).

There is no predictability to the timing or variation in dollar amounts of Davis-Bacon wage rate modifications. Surveys may be done frequently or not for many years. Some wage rates are changed in response to union collective bargaining agreements, but timing is also unpredictable. For example, there were 18 modifications to the "building" category wage rates in Montgomery County, Maryland, during 2014. Sometimes the modifications are so extreme, it renders a feasible development impossible. A September 2012 wage rate determination for a number of counties in Ohio increased a variety of trades' wage rates by 100 to 400 percent from the previous determination issued in 2010.

For these reasons, we urge interagency cooperation between HUD and DOL to permit borrowers on FHA-insured multifamily developments to lock in the wage rate determination for individual projects as early in the application process as possible. Developers and builders risk considerable sums up-front just in preparing an FHA application; once they have received a firm commitment, the mortgage amount is set, and it becomes time-consuming and costly to make changes.

An appropriate time for locking in Davis-Bacon prevailing wages for a new construction or substantial rehabilitation multifamily project is when HUD accepts a lender's application for a Firm Commitment. At the time HUD accepts a lender's application, it deposits the application fee and issues a receipt. The date on the receipt HUD issues to the lender should be accepted as a government source for a date-certain to lock in the current prevailing wage rates. NAHB continues urging DOL to change its policies, so HUD may lock in the Davis-Bacon prevailing wage rates at the time it accepts an application for a firm commitment of multifamily mortgage insurance for new construction or substantial rehabilitation.

Inclusionary Zoning

Inclusionary Zoning (IZ) requires a portion of new construction be designated as affordable housing for those with low-to-moderate income. Specifically, IZ policies typically require developers to subsidize a specified percentage of total units within market-rate developments and to set income-based price controls for the subsidized units. NAHB is concerned that there is too much focus on IZ as the single preferred method of achieving fair housing goals.

In the typical case where there are no or insufficient offsetting subsidies, IZ requires developers to lose money on some of the housing they build. This is effectively a tax, resulting in higher rents on non-subsidized apartments. In the NAHB-NMHC study, 30 percent of the multifamily projects were subject to IZ or similar "affordability" mandates. In these cases, IZ accounted for 5.7 percent of development costs on average, enough to cause a substantial increase in rents.

The reality is that different market segments may require different tools for improving affordability, from direct or indirect subsidies at the low end of the income bracket to better planning for housing and regulatory barrier removal strategies at the upper end of the income range. An economic study conducted for NAHB that focused on price and production effects concluded that in places like California, there was not an overall increase of housing production from IZ, and that IZ acts like a tax on housing.

The middle class gets squeezed out under IZ. Due to an increase in the cost to cover subsidized IZ units, the middle class is no longer able to afford the market-priced units and they are ineligible for the subsidized rates. IZ simply shifts the burden without solving

the long-term affordability issues.

IZ may be feasible if the right incentives are available. There are other approaches such as planning and zoning changes to assess development capacity and encourage affordable housing. Expedited permitting processes and advocacy efforts to reduce NIMBYism can also have broad effects on housing affordability.

NAHB urges government to encourage and coordinate with, and not prescribe to, local communities to adopt long-term comprehensive plans that will meet the demand for new housing and economic development. Eliminating exclusionary planning and zoning practices will encourage the production of the full range of housing options for all members of the community.

Fair Housing

NAHB supports the goals of the Fair Housing Act, as amended, to protect individuals' ability to own or rent property free from discrimination and ensure that those individuals have equal access to housing, regardless of race, color, national origin, religion, sex, disability, and familial status. NAHB supports policies that allow all individuals the opportunity to pursue their American Dream and seek the housing of their choice while allowing its members to develop and build safe and affordable housing in all areas where it is needed.

Furthermore, NAHB urges Congress to pass legislation that reduces barriers to, and supports the development of, much needed affordable housing and to provide clear exemptions from liability under the Fair Housing Act, where such liability may arise from good faith unintentional acts in pursuit of compliance with the requirements of local, state and federal housing programs. NAHB resolves to work with HUD staff to help the Agency clarify rules for preventing discrimination in accordance with the Fair Housing Act.

Affirmatively Furthering Fair Housing

I would also like to take a moment to discuss NAHB's position on HUD's Affirmatively Furthering Fair Housing (AFFH) Rule, which became effective Aug. 17, 2015. It requires states, local governments and public housing agencies to conduct a formal fair housing planning process as a condition of receiving certain HUD funds, such as the HOME Investment Partnership Program (HOME) and Community Development Block Grant (CDBG) Programs.

Many of NAHB's multifamily builders often encounter fierce opposition to their projects, especially when they attempt to build in more affluent areas. In fact, the NAHB-NMHC study found that 85 percent of the developers surveyed experienced added costs or delays due to neighborhood opposition to multifamily construction.

NAHB supports the rule's goals of reducing concentrations of poverty and housing segregation as well as providing greater economic opportunity to all residents in a community. The rule may help remove some barriers to affordable housing, but in its current form, the AFFH regulation could pose further challenges to producing and preserving affordable housing. NAHB is concerned that this initiative could have the unintended consequences of the federal government dictating prescriptions for land use and program design. Because HUD has authority to withhold housing funds from areas whose fair housing plans were not accepted, the AFFH rule may also pressure local jurisdictions to undertake misguided and shortsighted quick fixes, such as inclusionary zoning, in order to ensure that federal grants and subsidies are not

disrupted, rather than pursuing solutions that are sustainable over the longer run. As one NAHB member noted, “Sometimes even the suggestion [of inclusionary zoning] is all the local government staff needs to run with a program, and to ‘get the housing done.’ They don’t realize how expensive, and hard it is to implement [inclusionary zoning] within a development.” NAHB also expressed concerns about the rule’s potential for inappropriate federal encroachment on legitimate business practices, such as a landlord’s refusal to accept rental subsidies.

Under the rule, local governments, states and public housing agencies must submit an Assessment of Fair Housing (AFH) analysis which:

- Examines fair housing data to identify patterns of racially concentrated areas of poverty and disproportionate housing needs;
- Prioritizes fair housing goals;
- Determines what actions are necessary to achieve those goals; and
- Sets a timetable for reaching them.

In May, HUD withdrew the Local Government Assessment Tool. HUD explained that it initially rejected about 35 percent of AFH plans submitted by local governments in 2017, and called the tool “inadequate to accomplish its purpose of guiding program participants to produce meaningful AFHs.” The Department committed to make it less burdensome and more helpful in creating impactful fair housing goals. In the absence of a working information collection device, program participants were directed to use the previous analysis of impediments to fair housing choice (AI).

On August 13, HUD published an Advanced Notice of Proposed Rulemaking inviting public comment on amendments to its AFFH regulation. The Agency requested comments on changes that minimize regulatory burdens, focus on positive results rather than analysis, provide greater local control and innovation, increase housing choice and supply, and more efficiently use HUD resources. NAHB will work with HUD in hopes of making constructive improvements to this regulation.

Other Factors That Inhibit New Multifamily Production

Unfortunately, burdensome regulations are not the only policies pushing construction costs higher and housing affordability lower. Multifamily builders are also struggling with the effects of tariffs placed on goods that are integral to construction. Shortages of skilled labor also cause delays and drive up costs.

Tariffs

In early 2017, the Trump Administration levied combined tariffs as high as 27 percent on softwood lumber imported from Canada. As a result, the cost of framing lumber spiked and has been as volatile as we’ve ever seen. These price increases have caused the market value of every newly built multifamily unit to rise $1,500.

But lumber isn’t the whole story, particularly for multifamily developers. Tariffs on steel have also had adverse effects on the industry. Earlier this year, tariffs and quotas on steel and aluminum were put in place in the name of national security. As a result of this policy, the price of structural steel, including beams used to frame taller multifamily projects, has increased 20 percent in 2018.

If President Trump decides to move forward with tariffs on $200 billion of Chinese imports, the effects would be dire. The list of goods that would see a sudden 25 percent tax increase includes countertops, nails, saws, light fixtures, wire, kitchen cabinets and almost everything else we use to build homes.

Taken together, the price of building materials has been rising two to three times faster than the rate of inflation over the last six months.

Labor Shortages

The NAHB/Wells Fargo Housing Market Index[7] from December 2017 indicated that the cost and availability of labor was the top problem for builders in 2017. Eighty-two percent of builders reported problems with the cost and availability of labor in 2017. Eighty four percent of builders cited labor shortages as the top problem they expected to face in 2018, placing this issue in a tie for first place with building material prices.

Simply put, the skilled labor workforce is aging, and not enough new workers are entering the trades. The result of this dynamic is a chronic labor shortage in the home building industry.

In response to President Trump's plan to expand workforce development, NAHB pledged to educate and train 50,000 new workers over the next five years for careers in the construction trades. NAHB's Home Builders Institute (HBI), our workforce development arm, offers youth and adult training programs across the country to provide students with the hands-on experience necessary to build careers in construction and related fields. HBI will expand training, certification and job placement programs for underserved and at-risk youth, transitioning military, veterans, ex-offenders and displaced workers.

Section 3 Program

HUD's Section 3 Program is a little-known program that has been on the books for well over 20 years but has been administered under an interim regulation since 1994.

"Section 3" refers to Section 3 of the Housing and Urban Development Act of 1968, as amended by the Housing and Community Development Act of 1992. An obscure HUD program usually associated with public housing, Section 3 requires recipients of certain HUD financial assistance (including HOME and CDBG), to the greatest extent possible, to provide job training, employment, and contract opportunities for low- or very-low income residents in connection with projects and activities in their neighborhoods.

Reports from NAHB members indicate that Section 3 requirements are not uniformly enforced across the country. Where it is enforced, some builders attribute increased costs, administrative burdens and project delays to the program's requirements. Although well-intended, HUD's plans for Section 3 could present serious unintended consequences, such as additional costs and project delays, for multifamily builders.

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[7] The NAHB/Wells Fargo Housing Market Index is a monthly survey of NAHB members designed to take the pulse of the single-family housing market. The survey asks respondents to rate market conditions for the sale of new homes at the present time and in the next six months as well as the traffic of prospective buyers of new homes.

NAHB has offered solution-oriented ideas that address the construction labor shortage and promote job opportunities for low-income men and women. NAHB urged HUD to develop strategic partnerships with job training and social skill-building specialists who will deliver employees from the local community trained in the skill appropriate for the job site. For instance, HUD could work in partnership with NAHB's HBI to offer youth and adult training programs across the country that provide students with the hands-on experience necessary to build careers in construction and related fields. NAHB also asserted that HUD should either require the local government to maintain and/or certify a list of Section 3 firms, or HUD should take on that responsibility. The onus should also be on HUD or the local government to verify the eligibility of a Section 3 business, rather than shunting that responsibility to the builder, general contractor or subcontractors. HUD's online Section 3 Business Registry is a positive first step. Unfortunately, HUD does not verify the self-certifications submitted by the businesses, and it cautions database users to perform due diligence before awarding contracts.

Although the status of Section 3 regulations have not changed at this time, NAHB continues to monitor this issue and remains engaged with the appropriate HUD staff.

Access to Credit

Affordable multifamily development is dependent on accessible financing options. Fannie Mae and Freddie Mac (the Enterprises), HUD, FHA, the Rural Housing Service (RHS) in the Department of Agriculture (USDA) and Ginnie Mae all play a significant role in providing various credit options to support affordable multifamily development. State and local housing finance agencies (HFAs) also are a source of affordable multifamily financing programs. These agencies have proven to be dependable sources of financing even when private market sources of multifamily financing have withdrawn from the market in adverse economic conditions.

The Enterprises' multifamily programs form the core of multifamily debt financing provided by major financial institutions. The range of products and business lines employed by the Enterprises allow a wide range of multifamily rental properties that provide housing for very-low to middle income households to be financed in the conventional market. In fact, the Federal Housing Finance Agency (FHFA) announced in November 2017 that Fannie Mae and Freddie Mac will be allowed limited re-entry into the LIHTC market as equity investors. Allowing Fannie and Freddie to compete with private investment capital is expected to increase competition for the credits and thereby increase the value of the credits, resulting in more capital and greater affordability for LIHTC projects in rural areas.

Ginnie Mae's guarantee of securities of eligible multifamily FHA insured loans and multifamily Rural Development (RD) loans guaranteed by the RHS is essential to affordable multifamily development. Together, these agencies provide crucial counter-cyclical support to the housing market, expanding in downturns and contracting when the market improves.

HFAs generally have a mission to provide funding to increase and sustain affordable rental options and homeownership. These agencies support low- and moderate-income renters and homebuyers, and/ or special populations such as first-time homebuyers, active military and veterans, police and teachers, individuals with disabilities, and homeless individuals. Their programs are funded primarily through tax exempt bonds, HUD's HOME, and LIHTCs.

Preserving all these financing options is critical to ensuring that developers of affordable multifamily housing units have steady and reliable access to affordable credit. NAHB urges lawmakers and regulators to consider the critical role these agencies and their programs play in the housing finance system as housing finance reform legislation and policies are considered going forward. Additionally, federal banking regulations, such as the High Volatility Commercial Real Estate rules, should be examined to ensure these regulations are not impeding the availability and affordability of credit for acquisition, development and construction financing for multifamily development projects.

Regulatory Reform Will Complement, but Not Replace Federal Multifamily Programs

Regulatory reform will help improve affordability, but it is not a substitute for a direct subsidy. While regulatory reform will help us lower development costs, to reach lower-income households, it is financially infeasible to construct new, unsubsidized affordable rental units without federal assistance.

NAHB's members utilize a number of single family and multifamily housing programs administered by federal agencies. While this list is not all-inclusive, it does represent the most important programs for our members and the modest income Americans they serve. The major federal programs most important to NAHB members include:

- Tax programs: Mortgage Interest Deduction, LIHTC, Mortgage Revenue Bonds, and Mortgage Credit Certificates;

- FHA Mortgage Loan insurance: Single family homeownership, Multifamily new construction and preservation (most notably Section 221(d)(4) for multifamily new construction and substantial rehabilitation and Section 223(f) for multifamily refinancing);

- HUD Block Grant Programs: HOME and CDBG;

- HUD Rental Assistance: Primarily Section 8 Project Based Rental Assistance (PBRA) and the Housing Choice Voucher (HCV) Programs; and

- RHS single family, multifamily (Section 515 direct loan and Multifamily Preservation and Revitalization Demonstration Programs), and Section 521 Rural Rental Assistance programs.

Each of these programs serves an important purpose. They are not interchangeable, but are complementary. Different strategies are necessary to meet the housing needs of households with different income levels and in different parts of America. The array of federal government programs that have been developed over the years in response to identified needs are essential elements in ensuring that there are affordable options for providing housing. Steps should be taken to make the operations of these agencies more efficient and effective.

As the subcommittee examines the cost of regulations in multifamily development, we also request your continued support for successful housing programs such as the Low Income Housing Tax Credit (LIHTC), and full funding for vital rental housing programs such as the Housing Choice Voucher Program, Project-Based Section 8 Rental Assistance, the HOME

Program, and the Rural Development Multifamily Programs.

Conclusion

NAHB thanks the subcommittee for the opportunity to testify. Whether they rent or own, Americans want to choose where they live and the type of home that best meets their needs. NAHB thanks the chairman and this subcommittee for their leadership on this important issue, and stands ready to work with you to achieve necessary reforms and expand the availability of affordable housing.

In closing, NAHB would also like to applaud the New Democrat Coalition for releasing a white paper which seeks solutions to chronic problems facing the housing industry.
In crafting the document, the New Dems worked closely with NAHB and highlighted leading factors hindering new construction. This paper is an important step towards ensuring housing issues are kept a priority in Congress, and NAHB looks forward to continuing to work with them.

Thank you again, Mr. Chairman for the time and effort you devoted to the important issue.

Multifamily Cost of Regulation

2018 Special Study

Paul Emrath, National Association of Home Builders
Caitlin Walter, National Multifamily Housing Council

Regulation: Over 30 Percent of the Cost of a Multifamily Development

June 12, 2018

Paul Emrath, National Association of Home Builders
Caitlin Walter, National Multifamily Housing Council

Many Industry experts have become concerned about affordability of rental housing in America, and how difficult it has become to address the problem through new construction. According to the report on America's Rental Housing 2017 published by the Joint Center for Housing Studies at Harvard University, "The lack of new, more affordable rentals is in part a consequence of sharply rising construction costs, including labor and materials." The Harvard report goes on to say, "Tight land use regulations also add to costs by limiting the land zoned for higher-density housing and entailing lengthy approval processes."

Recently, the National Association of Home Builders (NAHB) and the National Multifamily Housing Council (NMHC) undertook a joint research effort to find out how much government regulation adds to the cost of building new multifamily housing. Results show that well over 90 percent of multifamily developers typically incur hard costs of paying fees to local jurisdictions, both when applying for zoning approval, and again when local jurisdictions authorize the construction of buildings.

However, government regulation can impose costs in other ways as well. Over 90 percent of multifamily developers also incur costs of delays caused by sometimes lengthy approval processes, development standards that go beyond what would ordinarily be done, changes to building codes over the past decade, and OSHA requirements. Other regulations, such as requiring developers to dedicate land to the government, are somewhat less common, but can be quite costly when they are encountered. The bottom line is that regulation imposed by all levels of government (whether local, state or federal) accounts for 32.1 percent of the cost of an average multifamily development.

A substantial amount of regulation is well intentioned and some of it undoubtedly serves a worthwhile purpose. Few would argue, for example, that basic safety standards for structures and workers are unnecessary. But regulation that exceeds 30 percent of a project's development costs raises questions about how thoroughly governments are considering the consequences of their actions. Are they aware of how much regulation currently exists? Do they realize how multiple regulations with conflicting standards can cause delays and increase costs? And do they understand the extent to which these increased costs translate into higher rents and make it difficult to build new housing that families with modest incomes can afford?

Survey Design

While the assertion that regulations increase the cost of multifamily development is commonly heard, the extent to which this happens is not easy to measure, and currently does not exist on a national scale. The only way to gather data that is at all comprehensive is from multifamily developers, as they are the only ones who experience a wide range of the various forms regulation can take. NAHB and NMHC set out to accomplish this through a survey of both memberships. The purpose of the survey was to quantify how much regulation exists and how much it is adding to the cost of developing new multifamily properties.

Multifamily developers do not, in general, have accounting systems designed to tease out these regulatory costs. So NAHB and NMHC crafted questions that most developers would be able to answer. The questions asked developers about the typical projects they build. The questions covered various delays and costs incurred at different stages of the development process. Developers were asked to provide all hard costs as a percent of total development cost for their typical projects (see Appendix 2).

The survey was conducted in the fourth quarter of 2017. A total of 40 usable responses were received from multifamily developers, evenly split between NAHB and NMHC members (with no duplication). The developers who responded reported building multifamily projects in all regions of the country, and the typical projects they build vary widely: from fewer than 5 apartments to more than 400, and from under $2 million in total development costs to more than $100 million.

NMHC and NAHB combined the results with information from other survey collections and public data sources, such as typical terms on construction loans and the average time it takes to complete different phases of a project, to estimate the final costs (see Appendix 1).

Types of Regulation

Regulatory costs fall into several categories—fees, development standards, building codes, land dedicated to public purposes, etc. The range of these regulations can be broad, and the cost of complying with them substantial. Figure 1 shows the incidence of different types of regulations imposed on multifamily developers, as well as the average cost of complying with those regulations when they do exist.

Figure 1: Incidence and Typical Magnitude of Regulatory Costs

Type of Cost	Share of Developers' Projects Subject to the Cost	Average Cost When Present (as a Share of Total Development Costs)
Cost of applying for zoning approval	98%	4.1%
Interest costs on refundable fees charged when site work begins	50%	0.5%
Other (non-refundable) fees charged when site work begins	93%	4.5%
Development requirements that go beyond the ordinary	95%	6.3%
Land dedicated to the government or otherwise left unbuilt	50%	4.3%
Fees charged when building construction is authorized	93%	4.2%
Cost of complying with affordability mandates (e.g., inclusionary zoning)	30%	5.7%
Cost increases from changes to building codes over the past 10 years	98%	7.2%
Cost of complying with OSHA requirements	90%	2.6%
Pure cost of delay (i.e., even if regulation imposed no other type of cost)	98%	0.7%

The first significant interaction between a multifamily developer and the government usually occurs when the developer applies for zoning approval to allow multifamily housing to be built on a particular parcel of land. The U.S. Constitution gives states the authority to regulate land use; and, although states sometimes try to influence land use patterns in various ways, they most often leave this up to local governments. Local governments, in turn, pass zoning ordinances that divide their territories into districts and specify how land in each district can be used (single-family versus commercial versus multifamily, for example). It's not impossible for a developer to acquire land that allows multifamily structures to be built on it without going through a rezoning process or obtaining some type of exemption to an existing ordinance, but this is the exception rather than the rule.

The typical projects of almost all the respondents (98 percent) were subject to costs at the zoning approval stage. When they exist, these costs average 4.1 percent of the total development costs. Regulatory costs incurred at this stage can include fees paid directly to a government, but may also include other types of costs. For example, the developers may have to pay for environmental impact, archeological or other types of studies.

Although local governments have the authority to approve development, existing environmental laws also give a role to the federal government. A developer may need to obtain a wetlands, stormwater and/or endangered species-critical habitat permit, each of which is overseen by a different federal government agency. Many states manage the wetlands permits under federal guidance, and states and local jurisdictions may have their own sets of requirements. Indeed, it can be difficult to identify which level of government is ultimately responsible for some regulation, and trying to reconcile conflicting requirements is one factor that can drive up the cost of compliance.

It is also common for governments to impose fees on a multifamily development when site work begins. Many communities charge impact, utility hook-up and other fees at this point. Impact fees are fees that are charged only on a new development and are supposed to be used only for capital improvements. State legislation establishes the types of impact fees local governments can charge. Examples are impact fees for the construction of new schools, roads, water facilities, sewer facilities, stormwater management, parks, fire, police, libraries, solid waste management, and general government. Some states allow all of these, while a select few of states do not allow them, such as Virginia. There are consultants who travel the country and specialize in calculating the maximum impact fees local governments can legally charge. Moreover, as a recently published University of California, Berkeley paper documented, cities often charge additional fees, negotiated on a case-by-case basis at different points in the development process, to allow a project to be built.

According to the 2012 Census of Governments, there are roughly 90,000 local governments in the U.S., and a particular development may be subject to fees from more than one of them—for example, from a municipality, a water district, and a school district with overlapping jurisdictions. The overwhelming majority (93 percent) of the typical projects of multifamily developers in the NAHB-NMHC survey pay fees at this stage of the process. When they exist, these fees average 4.5 percent of total development costs.

Some local governments charge developers guarantee or other fees that are refundable when the project is completed. Although these fees are also usually imposed when site work begins, the survey treats them separately, due to the different cost implications. If the fee is eventually refunded, the developer ultimately pays only the interest that accrues on the development and construction loans until that happens. Half of respondents' typical projects were subject to these fees; which, when present, averaged half a percent of the total development cost.

Many local governments require new development to conform to community design standards. This may include standards for streets and sidewalks, parking, height of buildings, landscaping and the architectural design of individual buildings. These standards impose little extra cost if they don't significantly exceed the developer's ordinary practices. In the absence of regulation, for example, developers will still ordinarily provide spaces for walking and parking, landscaping, and employ architects who attempt to design buildings that are attractive to potential tenants. The NAHB-NMHC survey asked multifamily developers specifically about the cost of standards that go beyond what they would otherwise do.

Almost all (95 percent) of the typical projects of the developers surveyed were subject to design standards that that go beyond what the developer would otherwise do. When these beyond-ordinary requirements were present, they accounted for an average of 6.3 percent of the overall development cost. Energy efficiency is a worthwhile objective, but NMHC and NAHB have argued that the up-front cost needs to be kept within reasonable bounds. NMHC and NMHC have supported some recent changes to the IECC but opposed others as not cost-effective. Not surprisingly, manufacturers of building products advocate for code changes that mandate more use of their products, and tend to be less concerned than NMHC and NAHB about costs. Past analysis by NMHC on previous code cycles (which remain in effect in many states) has shown that changes to the IECC have the potential to drive up construction costs by over $3,000 per apartment (depending on type of building and climate zone) and argued that subsequent savings on utility bills come nowhere near justifying the cost.

Half of the typical projects required developers to dedicate land to the government or otherwise leave it unbuilt. This requirement can take many forms, such as creating a park on the property or reserving part of the property for the government to use in some way. In these cases the developer must pay for the land but is not allowed to derive revenue

from it, driving up the cost per unit for the housing that can be built. For those projects subject to this regulation, it represented an average of 4.3 percent of total development cost.

Almost all of respondents (93 percent) paid some sort of fee when construction in their typical project was authorized. This could be limited to a building permit fee, but additional impact, hook-up or other fees may also be charged at this point. When they exist, the fees charged at this point average 4.2 percent of development costs, large enough to suggest that they often encompass more than the building permit fees.

Local jurisdictions are increasingly beginning to consider imposing affordability mandates to attempt to create new affordable housing. These mandates without any offsetting incentive like a tax exception typically create few units and effectively tax some housing units (and their occupants) to subsidize others. The easiest way to see this is in cases where developers pay a fee to avoid the requirement—that amount gets added to the overall amount the developer must pay, thus raising the rents required. But even if they don't pay a fee, the regulation may require them to lose money on some of the housing they build, which is effectively a tax, resulting in higher rents on non-subsidized apartments. Almost one-third (30 percent) of developers who responded indicated that their typical projects incurred costs related to complying with such mandates. These costs, when they exist, averaged 5.7 percent of total development costs, enough to result in substantially higher rents.

The NAHB-NMHC survey also asked developers about the cost implications of changes to building codes over the past ten years. Most jurisdictions have been enforcing building codes for decades, and the codes have been updated and refined many times over that span. Most have adopted a version of national model codes, which have been in widespread use since the 1950s. These are updated every three years, and the number of refinements considered and voted upon during each three year cycle runs into the thousands.

Virtually no one would argue against public standards for basic soundness and safety of residential structures, but over the decades codes have expanded well beyond this and are increasingly being used as a vehicle to advance various policy objectives. A leading example is energy efficiency. There is now a model International Energy Conservation Code® (IECC).

Energy efficiency is a worthwhile objective, but NMHC and NAHB have argued that the up-front cost needs to be kept within reasonable bounds. NMHC and NMHC have supported some recent changes to the IECC but opposed others as not cost-effective. Not surprisingly, manufacturers of building products advocate for code changes that mandate more use of their products, and tend to be less concerned than NMHC and NAHB about costs.

This is another area where the federal government has become increasingly involved. The Environmental Protection Agency, the Federal Emergency Management Agency, and the Department of Energy (DOE), all actively participate in the development of national model codes, proposing changes to national model codes and testifying in favor of them during code hearings. DOE also has a share of its budget set aside for persuading state and local jurisdictions to adopt more stringent codes. Representatives from NAHB who witnessed all of the recent code hearings have criticized federal agencies for supporting certain code changes that removed flexibility and limited builders' options, driving up costs without improving energy efficiency, to the benefit of specific product manufacturers.

Nearly all (98 percent) of developers said changes in building codes over the past 10 years increased development costs in their typical projects, and these costs, when they exist, average 7.2 percent of total development costs.

Nine out of ten developers said complying with requirements of the Occupational Safety and Health Administration (OSHA) increased costs in their typical projects, and these costs, when present, average 2.3 percent of total development costs. Again, few would argue that safety standards for construction workers are unnecessary. In recent years, however, OSHA has issued a substantial number of regulations imposing costly compliance requirements all without providing any evidence that they would actually improve safety in the residential construction industry. In the Beryllium rule, for example, the evidence of a health risk came from workers in manufacturing industries or performing abrasive blasting activities. In the Volks rule, OSHA was criticized as doing little beyond driving up record keeping costs for businesses (and possibly violating the statute of limitations in the process).

Even when regulation imposes no direct costs, it can have a financial impact if it delays the development and construction process. If it takes longer to begin leasing and earning income on a property, it will take longer to pay off any development and construction loans and more interest will accrue.

Some regulatory delay is inevitable, as it will naturally take some time for local building departments to review and approve plans and respond to requests for inspections. Precisely how long it is reasonable for a developer to wait for approvals and inspections is open to debate, but there are examples that clearly seem excessive. One academic study, for example, found that it took an average of 788 days to prepare a submission and receive approval for an individual federal wetlands permit.

Virtually all the developers (98 percent) said complying with regulations caused some sort of delay for their typical projects. For these projects, NMHC and NAHB estimated that average additional interest was 0.7 percent of total development costs. This is a "pure" cost of delay that regulation would cause even if it imposed no other type of cost. It is calculated by subtracting every other type of regulatory cost, then estimating the additional interest accruing on the share of the remaining development cost that is typically financed.

Total Cost of Regulation

To estimate how much in total the government regulations described above add to multifamily development costs, it is necessary to take both the incidence and magnitude of the various types of regulation into account—in other words, to average in the "zeroes" when a particular regulation does not apply. Figure 2 shows that, when this is done, the listed categories taken together on average account for 32.1 percent of development costs for a multifamily project.

Among the listed categories, average cost is highest for changes to building codes over the past 10 years (7.0 percent of total development costs), followed by development standards imposed by government that go beyond what the developer would ordinarily do. It is interesting that government control over how a project is built can be more costly than actual fees charged, but unsurprising given that they can be time consuming and thus cost more.

Figure 2: Government Regulation as a Share of Multifamily Development Costs

Type of Cost	Lower Quartile	Average	Upper Quartile
Cost of applying for zoning approval	1.1%	4.0%	5.3%
Interest costs on refundable fees charged when site work begins	0.0%	0.2%	0.2%
Other (non-refundable) fees charged when site work begins	1.9%	4.2%	5.5%
Development requirements that go beyond the ordinary	1.1%	5.9%	8.4%
Land dedicated to the government or otherwise left unbuilt	0.0%	2.1%	3.3%
Fees charged when building construction is authorized	1.1%	3.9%	5.4%
Cost of complying with affordability mandates (e.g., inclusionary zoning)	0.0%	1.7%	2.6%
Cost increases from changes to building codes over the past 10 years	5.2%	7.0%	7.1%
Cost of complying with OSHA requirements	1.3%	2.3%	2.3%
Pure cost of delay (i.e., even if regulation imposed no other type of cost)	0.1%	0.7%	1.2%
TOTAL ESTIMATED REGULATION AS A SHARE OF DEVELOPMENT COSTS	**21.7%**	**32.1%**	42.6%

Affordability mandates, when they exist, are nearly as costly as relatively recent changes to building codes and beyond-ordinary development starts, but overall have a smaller average impact on costs because they are encountered less frequently. In contrast, regulatory delays are encountered very frequently, but have a comparatively small average impact on costs because they are limited to the extra interest that accrues on development and construction loans.

Refundable fees have the smallest impact of any of the types of regulatory costs listed, both because they apply only half of the time and because they are limited to the interest that accrues until they are refunded.

To illustrate the variability in regulatory costs, in addition to averages, Figure 2 shows the upper and lower quartiles (costs are below the lower quartile for 25 percent of respondents, and above the upper quartile for 25 percent). While on average regulation accounts for 32.1 percent of total multifamily development costs, the quartiles give a range of 21.7 to 42.6 percent.

Although the cost components sum to the bottom line total for the averages in Figure 2, the components of the upper and lower quartiles do not. The ten components in the "lower quartile" column in particular sum to considerably less than 21.7 percent. The implication is that multifamily developers can minimize some types of regulatory costs depending on where they operate—but not all of them proportionately at the same time.

Costs Not Captured

Although the NAHB-NMHC survey sought to be as comprehensive as possible, the above results do not capture everything. Some government actions impact development costs in a way a multifamily developer can't reasonably be expected to quantify. For example, federal immigration policy may affect the supply of construction labor, and tariffs can affect prices of building materials like lumber[1] and steel. Developers do not in general have a way of evaluating how much the prices they pay for labor and materials are influenced by these federal policies.

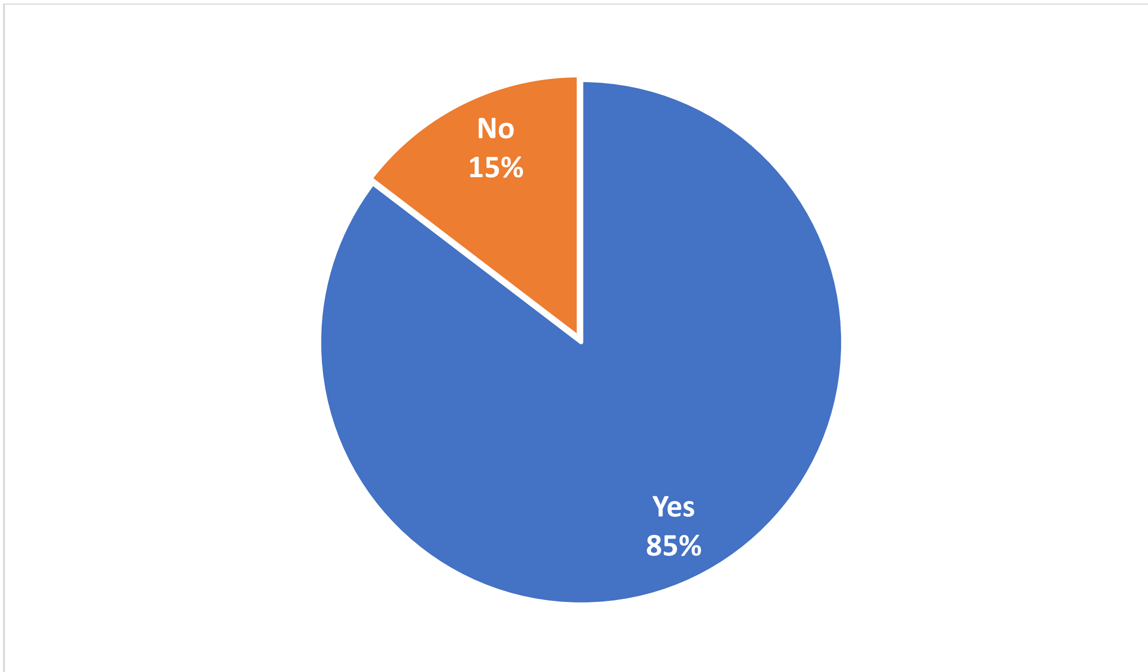
The survey asked developers about delays due to government regulation, but there can be multiple reasons for those delays not all unambiguously tied to a government action. One is neighborhood opposition to the development. At the local level, governments may encourage or facilitate local groups who oppose multifamily development. An obvious way to do this is by allowing local groups to sue any developer who proposes to build multifamily housing, but there are many more subtle ways to encourage opposition.

A developer may have to devote time and financial resources to deal with this opposition, by meeting with local groups before seeking zoning approval, for instance. To quiet the opposition, developers may find it necessary to make concessions to local groups, such as reducing size of the buildings so that land costs are allocated to fewer apartments and cost per apartment is increased. In an extreme case, local opposition may be able to cause a local government to reverse its decision to approve a project after the developer has already invested heavily in it. In many of these cases, there is an obvious cost to neighborhood opposition, but how much responsibility the local government bears for it may not always be clear. It is not uncommon for developers to hire consultants to debunk claims made by opposition to a project.

Figure 3 below shows that the overwhelming majority (85 percent) of the developers responding to the NAHB-NMHC survey have experienced added costs or delays due to such opposition.

[1] The effects of the current lumber tariffs are estimated in Impact of the Canadian Lumber Duties on the U.S. Economy in 2018.

Figure 3: Have you experienced added costs or delays due to neighborhood opposition to multifamily construction?

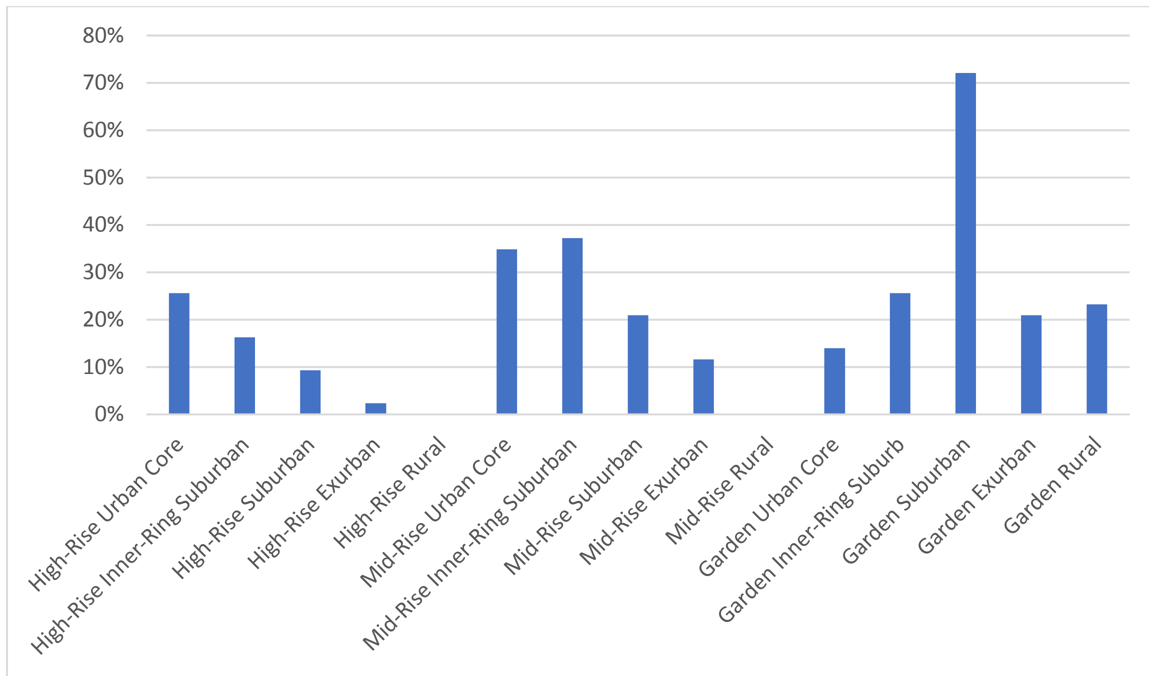


Profile of Respondents and Their Typical Projects

The range of costs highlights that not all development projects are the same. Costs can vary by jurisdiction, as well as by geographic location and type of project—garden apartments on undeveloped land can be much less complicated to build than a high-rise in an urban area, for example. Respondents were able to choose more than one option as to their typical project type.

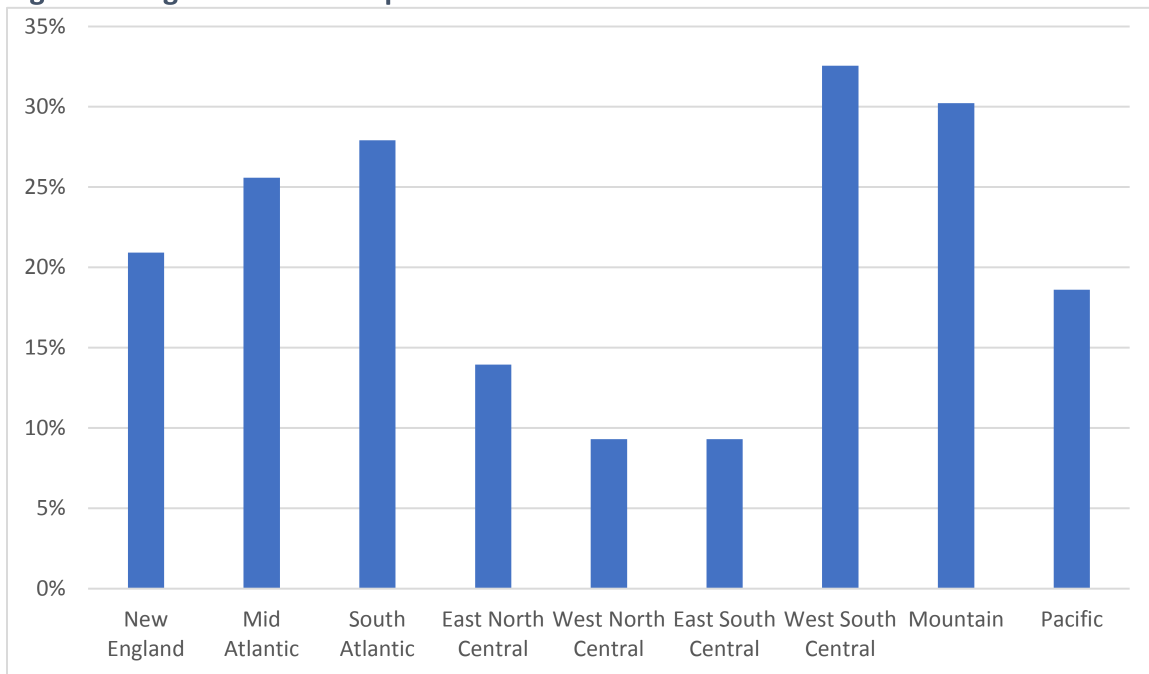
Respondents built a variety of product types that also varied by location (see Figure 4). The most common type of project was a garden development in the suburbs (72 percent). Mid-rise projects were the next common, with 35 percent building mid-rise developments in urban areas, and 37 percent building similar projects in inner-ring suburbs. About one-quarter (26 percent) of developers reported that they typically build high-rise apartments in urban settings.

Figure 4: Type and Location of Multifamily Projects



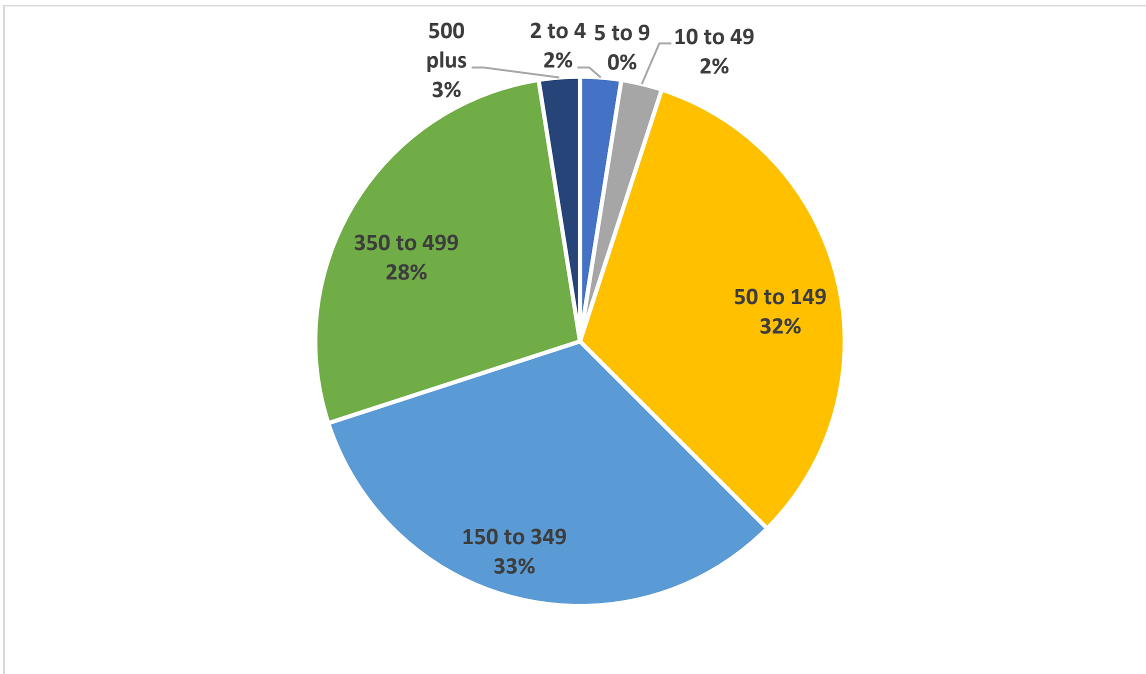
All regions of the United States were represented in the survey sample as well. The largest percentage of developers operated in the West South Central (33 percent) and Mountain (30 percent) regions (see Figure 5). The South Atlantic and Pacific regions featured the highest distribution of multifamily permits in the U.S. in 2017 and had the third and fifth largest distribution of respondents, respectively.

Figure 5: Regions Where Respondents Build



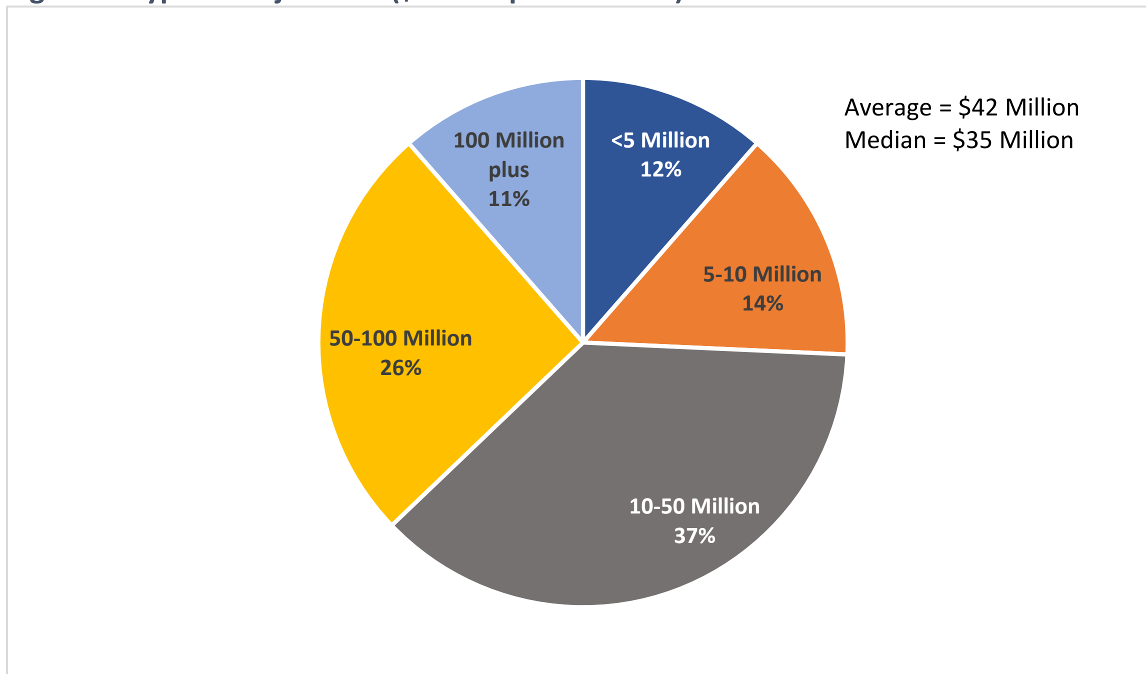
A fairly wide range of typical development size was represented by respondents as well (Figure 6). A small portion of respondents (4 percent) typically built projects fewer than 50 units or greater than 499 units (3 percent), while the remaining respondents were relatively evenly split between 50 to 149 units (32 percent), 150 to 349 units (33 percent), and 350 to 499 units (28 percent).

Figure 6: Typical Project Size (No. of Units)



In terms of financial costs, the cost was even more widely distributed (see Figure 7). The average cost of a typical development project for these developers was $42 million. Over one-third (37 percent) of respondents had a typical project size of $10-$50 million.

Figure 7: Typical Project Size ($Development Costs)



Summary and Conclusion

As the above discussion has demonstrated, multifamily development can be subject to a bewildering array of regulatory costs, including a broad range of fees, standards, and other requirements imposed at different stages of the development and construction process. In view of this, it may not be surprising that regulation imposed by all levels of government accounts for 32.1 percent of multifamily development costs on average, and one-fourth of the time reaches as high as 42.6 percent.

Although local governments generally have authority for approving development and adopting building codes, state and federal governments are becoming increasingly involved in the process. Sometimes the federal involvement is readily apparent, as when issuing stormwater permits or enforcing OSHA requirements. At other times, the federal involvement is less obvious. Examples include federal participation in model building codes, and attempts to influence local development through conditions for obtaining grants or other sources of funding. Indirect influences like these sometimes make it impossible to untangle which level of government is ultimately responsible for a given dollar of regulatory cost.

The current estimate that government regulation accounts for 32.1 percent of total development costs is almost certainly understated to some extent, as it was not possible to account for items like the effects of tariffs on building materials or the extent to which local jurisdictions may empower their citizens to oppose multifamily housing in their communities. Average costs could be even higher now or in the near future due to regulations taking effect since the multifamily projects in the survey were completed. For example, OSHA's Silica Rule went into effect in late 2017, a regulation that industry groups have criticized as unreasonably onerous and unnecessarily costly. Similarly, local jurisdictions are just beginning to adopt the 2018 versions of the model international building codes. Home Innovation Research Labs has recently estimated that the difference between the 2018 and 2015 versions of the codes can add thousands of dollars onto the cost of a multifamily building. As is typically the case, federal agencies supported several of the cost-increasing changes to the codes.

When the cost of multifamily development rises, it unavoidably translates to higher rents and reduced affordability of rental housing. Multifamily developers can not secure financing to build their projects unless they can demonstrate to lenders that the rents will be sufficient to cover costs and pay off the loans.

The purpose of this article is not to argue that all regulation is bad and should be eliminated, but to raise awareness of how much regulation currently exists, how much it costs, and to encourage governments to do a thorough job of considering the implications for housing affordability when proposing and implementing new directives.

Appendix 1:
Assumptions Used in the Calculations

In order to calculate a final effect on development costs, many of the NAHB-NMHC survey responses need to be combined with additional information. Primarily these are assumptions about the terms of development and construction loans, and how long construction typically takes, and how to allocate costs to different stages of the development and construction process. This appendix lists all the assumptions used in the calculations and gives the sources for each.

Loan terms

1.0 point charged for all land acquisition, development, and construction (AD&C) loans, based on results from a Quarterly Finance Survey (QFS) that NAHB was conducting in the early to mid-2000s.

A 7.65 percent interest rate on all AD&C loans. The QFS indicates that rates are typically set one point above prime, and 6.65 percent is NAHB's estimate of the prime rate that would prevail in the long run under neutral Federal Reserve policy.

The estimates also assume that three-fourths of any category of costs are financed, based on typical AD&C loan-to-value ratios in the QFS.

Construction Lags

The source for information lags not directly collected in the NAHB-NMHC questionnaire is the Survey of Construction, conducted by the Census Bureau and partially funded by the Department of Housing and Urban Development. Preliminary estimates are taken from the published annual tables, averaged over the 2001-2016 period:

If project is 2-4 units
- Authorization to start = 1.71 months
- Start to completion = 10.87 months

If project is 5-9 units
- Authorization to start = 1.95 months
- Start to completion = 11.64 months

If project is 10+ units
- Authorization to start = 1.94 months
- Start to completion = 13.21 months

The NAHB-NMHC survey collected data on how much time regulation adds to the development process. To assign this to a particular phase of the development the following assumptions are used.

The regulatory delay is split and attributed half to the lag between applying for zoning approval and the beginning of site work, and half to the period after site work begins. If half of the regulatory delay exceeds the lag between applying for approval and beginning of site work, the excess is also attributed to the period after site work begins. It is first assumed that the resulting regulatory delay is

attributable to the period between the start of site work and the start of building construction, minus 3 months (the assumed minimum time it would take to do site work in the absence of regulation, based on conversations with developers). If any regulatory delay remains after being allocated to the zoning approval and site work periods, it is then attributed to the building construction period, and the start-to-completion lag is adjusted upward beyond the SOC-based average, accordingly.

The analysis assumes all loans are paid off when the buildings are completed.

Cost Breakdown

To implement the process described in the paragraph above and calculate a "pure" cost of delay (i.e., the effect regulatory delay would have even if the regulation imposed no other cost), estimates of costs incurred during different phases of the development process are needed.

The breakdown is based on the split between lot and construction costs in NAHB's Construction Cost Surveys (averaged over surveys conducted since 2000) and the Census Bureau's "noncostruction cost factor" for raw land. The calculations also assume three-fourths of these costs are financed, based on typical AD&C loan-to-value rations in the QFS.

Resulting assumptions:

- Only the cost of applying for zoning occurs at the very start of the development process. Financing costs associated with this are charged are to the regulatory cost of the application and not counted in the pure cost of delay.
- 10.2 percent of total development represent costs financed by a land acquisition loan at the start of the site work phase.
- 10.8 percent of total development costs represent costs financed by a development loan during the site work phase, assuming draws on the loan occur on average halfway through this phase.
- 54.0 percent of total development costs represent costs incurred after building construction has started and financed with a construction loan, again assuming draws on the loan occur on average halfway through the site work phase.

Appendix II.

NAHB-NMHC Multifamily Regulations Cost Survey Questionnaire

1. What type of multifamily projects do you typically build in what areas? ***Select all that apply***

	Urban Core	Inner-Ring Suburban	Suburban	Exurban	Rural
High-Rise	☐	☐	☐	☐	☐
Mid-Rise	☐	☐	☐	☐	☐
Garden/Low-Rise	☐	☐	☐	☐	☐

2. What regions do you build in? Please select all that apply.

- ☐ New England (CT, ME, MA, NH, RI, VT)
- ☐ Mid Atlantic (NJ, NY, PA)
- ☐ South Atlantic (DE, DC, FL, GA, MD, NC, SC, VA, WV)
- ☐ East North Central (IN, IL, MI, OH, WI)
- ☐ West North Central (IA, KS, MN, MO, NE, ND, SD)
- ☐ East South Central (AL, KY, MS, TN)
- ☐ West South Central (AR, LA, OK, TX)
- ☐ Mountain (AZ, CO, ID, NM, MT, UT, NV, WY)
- ☐ Pacific (AK, CA, HI, OR, WA)

3. Including units you may start before the end of the year, how many multifamily units will your company start in 2017? ____________________

When answering this survey, please refer all your answers to the typical (most common) multifamily project your company builds.

Respond only for your local office/division, if you are part of a larger company.

4. How many units does your typical project have?

- ☐ 2-4 units
- ☐ 5-9
- ☐ 10-49
- ☐ 50-149
- ☐ 150-349
- ☐ 350-499
- ☐ 500 units or more

5. What is the total dollar amount spent on development costs in your typical project?

$____________________

Land Use & Planning Regulations

6. For a typical piece of land, how much does it cost to apply for zoning approval as a % of total development cost? *(Include costs of fiscal or traffic impact or other studies, and any review or other fees that must be paid by time of application. Please enter "0" if application costs are Zero percent).*

____________________**%**

7. For a typical project , how many months does it take between the time you apply for zoning approval and the time you begin site work?

___________________months

8a. When you begin site work, do you pay any guarantee or other fees that are refundable when the project is completed?

☐ Yes ☐ No

8b. If "yes" in question 8A, how much are those refundable fees, as a % of total development costs?

___________________%

9. Other than the refundable fees mentioned in question 8a, how much does it cost to comply with regulations when site work begins, as a % of total development costs? *(Include costs of complying with environmental or other regulation as well as the cost of hook-up or impact or other fees.) Please enter "0" if cost of complying with these regulations is Zero percent).*

___________________%

10. How much do development requirements that go beyond what you would otherwise do (in terms of property layout, landscaping, materials used on building facades, etc.) add to your cost, as a % of total development costs? *(Please enter "0" if the jurisdiction's requirements don't go beyond what you would normally do).*

___________________%

11. In the typical case, what is the value of any land that must be dedicated to the local government or otherwise left unbuilt (for parks, open green space, etc.), as a % of total development cost? *(Please enter "0" if dedicating land is required infrequently).*

___________________%

12. How many months does it take between the time you begin site work and the time you obtain authorization to begin construction of the apartment building(s)?

___________________ months

13. How much extra time (in months) overall does complying with regulations add to the development process? *(Please enter "0" if regulations typically cause no delay).*

___________________months

14. When you obtain authorization to begin construction, how much do you pay in additional fees, as a % of total development costs? *In many cases, this will be only a permit fee, but include any additional impact or hook-up or inspection fees if they kick in at this time. (Please enter "0" if fees paid during or after construction are Zero percent).*

_________________%

15a. In the typical case, does a jurisdiction have inclusionary zoning/affordable housing requirements that apply to your project?

☐Yes ☐No

15b. In the typical case, how much do these requirements (or a fee in lieu of affordable housing) cost as a percent of total development costs? (*Please enter "0" if inclusionary zoning/affordable housing mandates/fees in lieu of affordable housing are encountered infrequently).*

_________________%

Construction/Building Regulations

16. Over the past 10 years, how much have changes in construction codes and standards added to the cost of building a typical multifamily project, as a % of total development costs? *(Please enter "0" if code changes have had minimal impact on costs).*

__________________%

17. How much does complying with OSHA or other labor regulations cost, as a % of total development cost? *(Please enter "0" if labor regulations have no impact on development costs).*

___________________% ☐ Don't know/use of subs makes it impossible to estimate

18. Have you experienced added costs or delays due to neighborhood opposition to multifamily construction?

☐ Yes ☐ No