

# Producing Affordable Housing in Rising Markets: What Works?

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*The analysis and conclusions set forth in this article are solely the responsibility of the authors and do not indicate concurrence by the Board of Governors of the Federal Reserve System.*

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## Abstract

*As cities across the United States have rebounded from the Great Recession, an increasing number of households in urban areas are facing high rent burdens in order to remain in their current neighborhoods. Several policy options have been used to maintain or increase the supply of below-market-rate housing, including inclusionary zoning (IZ), tax increment financing, and household-based subsidies such as vouchers. In this article, we describe the problem of affordability in rising markets and review existing evidence on how well local policy approaches work. The most widely used policies, local IZ and statewide “fair share” laws, have produced relatively small numbers of affordable units and are therefore unlikely to substantially mitigate the effects of rising housing costs. More effective policies to develop and preserve affordable housing, particularly in high-opportunity neighborhoods, will require increased public and private funding and political support.*

## Introduction

Gentrification in its classic form entails an influx of higher socioeconomic status individuals and investment into relatively poor neighborhoods that have experienced disinvestment. During the early waves of gentrification that were first noticed in the United States in the 1960s and 1970s, gentrification typically entailed the rehabilitation of older housing units (Spain and Laska, 1980). In recent decades, however, gentrification has also taken the form of “new build” housing where private developers build market-rate housing for an upscale clientele in formerly poor

neighborhoods (Davidson and Lees, 2010). The state, too, sensing an opportunity, has gotten in on the act—at times subsidizing housing development in neighborhoods ripe for gentrification (Wyly and Hammel, 1999). After decades of disinvestment and white flight in the mid-20th century, gentrification is like a magic elixir returning old central cities to the vigor of their youth. The elixir of gentrification is not without side effects, however. As higher-socioeconomic-status individuals and investment capital flow into formerly depressed neighborhoods, these same spaces become more valuable. More and wealthier people want to live there and are willing to pay a premium to do so. This demand translates into higher values for owner-occupied homes and higher rents for rental units. A neighborhood that formerly had an abundance of affordable housing is transformed to one where market-rate housing is no longer affordable. This transformation of the housing stock in gentrifying neighborhoods from relatively affordable to beyond the reach of those with modest means can pose a number of problems (Newman and Wyly, 2006).

Although gentrification might appear to offer a windfall for homeowners, gentrification can also cause challenges for some homeowners. Because local property taxes are typically a function of the market value of a property, rising property values in gentrifying neighborhoods often translates into rising property tax bills. For those on fixed incomes, these rising tax bills can render their homes too expensive. Instead of a windfall, property owners may find themselves unable to afford homes they purchased.

The impact of gentrification is perhaps most serious for renters. As a neighborhood gentrifies, the demand for housing there increases, leading to concomitant increases in rents. Current residents may find themselves no longer able to afford their current units or, if they choose to move, unable to afford to remain in their gentrifying neighborhood. Moreover, poor residents who may have considered moving into the formerly affordable neighborhood may find that option no longer available to them (Newman and Wyly, 2006).

The evidence on poorer residents being directly displaced from gentrifying neighborhoods is mixed. Studies have not typically found residential turnover among poorer residents to be substantially higher in gentrifying neighborhoods than in other poor neighborhoods that do not gentrify, as one would expect to find if gentrification led to elevated rates of displacement (Ellen and O'Regan, 2011; Freeman, 2005; Freeman and Braconi, 2004; Freeman, Cai, and Cassola, 2015; Lee, 2014; McKinnish, Walsh, and White, 2010; Vigdor, 2002). This finding may be because residential instability is high among poor residents and in poorer neighborhoods in general. Adding gentrification to the mix may not appreciably change the already high rates of displacement and residential instability among poor residents. Prior research has also shown that poorer residents are less likely to move into gentrifying neighborhoods (Lee, 2014; Quillian, 1999, 2003). This pattern is consistent with exclusionary displacement—when poorer households can no longer move into formerly affordable neighborhoods that have gentrified.

If gentrification does not necessarily lead to increased rates of direct displacement, it poses for localities at least two other challenges related to housing affordability. First, if gentrification causes exclusionary displacement, which the available evidence suggests, the housing affordability problem boils down to the location of housing that is affordable. The gentry moving into a particular neighborhood or neighborhoods and causing gentrification in those places should result in less pressure on housing in other neighborhoods, which could result in a mismatch between where

affordable housing is needed and where housing is becoming or remaining relatively affordable. In a few select cities (for example, San Francisco, California), gentrification pressures may be so great that virtually the entire city becomes prohibitively expensive. Declining affordability in gentrifying neighborhoods could prove disruptive for poor residents and for the businesses and services that relied on those residents as clientele (Meltzer, 2016; Parker, 2016). The decline in affordability associated with gentrification can thus impact cities in several ways. The gentrifying neighborhood may become unaffordable, disrupting the lives of long-term residents—even if they are not directly displaced. The supply of affordable housing may be to some extent relocated to other neighborhoods that may or may not be accessible to those who need such housing.

Beyond housing affordability, gentrification can also engender feelings of being “pushed out” among long-term residents. As used here, pushed out refers to the disempowerment felt by long-term residents in reaction to their neighborhood changing in ways over which they had little control or say and are ultimately not intended for their benefit. The new amenities, lower crime, and other changes are viewed as being for the benefit of the newcomers to the neighborhood. Over time, long-term residents may no longer feel welcome in their own neighborhood and may leave even if they are not forcibly evicted (Freeman, 2006).

Such feelings can motivate a backlash against gentrification or nearly any type of investment in poorer communities as residents fear the end result will be their being pushed out. This backlash can make much-needed redevelopment more difficult to accomplish in many cities.

The first wave of gentrification in the United States in the 1970s and 1980s was limited to a few neighborhoods in a few cities and was characterized as “islands of renewal in seas of decay.” The most recent wave of gentrification in the second decade of the 21st century appears to be more widespread and is affecting housing costs across wide swaths of cities. For example, a report by the Furman Center found that in most of the largest 11 metropolitan areas in the country, the number of rental units that were affordable to the typical renter fell between 2006 and 2014. Moreover, income growth lagged well behind the rise in rent levels in most of these 11 metropolitan areas (Ellen and Karfunkel, 2016).

Cognizant of the potential pitfalls of gentrification, a number of localities have adopted various policies to address the potential problems that arise with rising housing costs and loss of affordable stock. The increasing prevalence of gentrification in formerly poor neighborhoods together with the continued decline and disinvestment in other neighborhoods has created a mix of scenarios that call for different strategies to assist poor households in inner cities.

One approach in inner-city neighborhoods, where concentrations of poverty are high and prospects for upward mobility dim, is to increase residents’ access to areas with plentiful employment options and high-quality schools. The Moving to Opportunity (MTO) demonstration program, which provided housing vouchers to public housing families to move to low-poverty neighborhoods, is perhaps the most well-known example of this approach. For people to be able to move out, affordable options are needed in high-opportunity neighborhoods. The recently released U.S. Department of Housing and Urban Development (HUD) guidelines that call for local governments to “Affirmatively Further Fair Housing” and take steps to encourage economic and racial integration are also motivated, in part, by the goal of increasing minorities’ access to areas of high opportunity.

Another approach attempts to connect isolated pockets of concentrated poverty to the surrounding metropolis by developing mixed-income developments in these same neighborhoods and investing in support programs designed to foster upward mobility among poorer residents there. These efforts typically include investments in local schools, counseling and career coaching for adolescents, and support services for families. The Harlem Children's Zone and its imitator, the HUD sponsored Choice Neighborhoods Program, are both examples of this approach (HUD, 2016c).

Finally, many localities have adopted an approach that seeks to maintain affordability in places where housing prices are rapidly escalating or are at risk of doing so. Cities such as New York City, San Francisco, and Washington, D.C., are the epitome of "hot markets," where a desperate need exists for more affordable housing across the board. Other cities, which are perhaps not yet experiencing an across-the-board rise in housing prices, are still experiencing gentrification in some neighborhoods and the potential to experience broader rises in housing prices. This last approach of developing and maintaining affordable housing for cities confronting affordability challenges or foreseeing such challenges<sup>1</sup> is the focus of this article.

In the remainder of the article, we review existing evidence on the most widely used local and state policies that are intended to create affordable housing. The second section describes how these policies work and where they have been adopted. The third section summarizes evidence from prior studies on how much housing has been produced. The fourth section briefly reviews spillover effects of the policies on local housing markets. The final section concludes and offers policy recommendations.

## Context of State and Local Affordable Housing Programs

Affordable housing providers have for decades accessed a variety of federal resources to assist with affordable housing development and neighborhood revitalization. Two such programs are the Low-Income Housing Tax Credit (LIHTC) and the Housing Choice Voucher (HCV) Programs, which are discussed further in the remainder of this article. The LIHTC Program, the largest source of funds for affordable housing development, uses federal income tax credits to finance below-market-rate housing in localities across the United States. Most large cities and counties administer federally subsidized HCVs that assist low-income families to rent private market apartments. More broadly, housing and neighborhood revitalization activities are supported by numerous federal programs, such as HUD's Community Development Block Grant (CDBG) program, HOME Investment Partnerships Program (HOME), and Choice Neighborhoods; Treasury Department initiatives such as Community Development Financial Institutions and New Market Tax Credits; and U.S. Department of Agriculture programs supporting rural housing and community development. Local governments and nonprofit organizations often layer resources from several of these programs in order to finance affordable housing development, acquisition, or rehabilitation. Although the focus of this article is on state and local programs, federal support remains an important although declining component of the affordable housing ecosystem. For example, the growth of HUD's budget has failed to keep up with the growing size of the poor population (Dolbear and Crowley, 2007).

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<sup>1</sup> As Acolin and Wachter (2017) discuss, affordability challenges may become a widespread phenomenon in the new regime in which urban centrality is increasingly important.

Not-for-profits and foundations have also stepped into the gap left by the relative decline in federal funds for affordable housing. The Housing Partnership Equity Trust (HPET) is an example of such an effort. HPET is a social venture real estate investment trust owned by nonprofits and devoted to preserving affordable rental housing. The goal of the HPET is to raise a pool of capital that can be quickly deployed to acquire rental properties at risk of becoming unaffordable.

Several types of local and state policies are designed to produce or preserve affordable housing as the cost of market-rate housing increases. For purposes of this article, we define “affordable housing” broadly to mean any housing that (1) must be rented or sold at below-market prices, or (2) can be occupied only by households below a defined income threshold. We briefly describe several local and state policies designed to maintain or increase the supply of affordable housing and review existing evidence on the amount of affordable housing produced by these policies.

Most local affordable housing policies fall into one of two categories—those that require affordability through zoning or planning laws, and those that create a targeted local funding mechanism. As shown in exhibit 1, policies in both categories can take a variety of different forms.

The most widespread zoning-related policy is local inclusionary zoning (IZ), sometimes called inclusionary housing or incentive zoning. These policies require or give incentives for developers of market-rate housing to set aside some units at below-market rents or prices. The term “inclusionary” is intended as a countermand to traditional “exclusionary” zoning practices such as minimum lot sizes that restrict housing density, thus increasing average housing development costs (Glaeser, Schuetz, and Ward, 2006; Malpezzi, 1996). Although referred to collectively, local IZ policies vary considerably in design along multiple dimensions. A few key characteristics include (1) whether they are mandatory or voluntary, (2) what size or type of development projects are affected, (3) the required share of affordable units, (4) the income of eligible residents, (5) the length of affordability restrictions, and (6) the availability of cost offsets such as density bonuses (Schuetz, Meltzer, and Been, 2009). No comprehensive inventory of IZ policies exists, but researchers have estimated that more than 200 cities, counties and towns across the United States have adopted some form of local IZ (Mukhija et al., 2010; Schuetz, Meltzer, and Been, 2011). IZ is particularly popular among local governments in the San Francisco Bay Area, Southern California, Massachusetts, the New York City metropolitan area, and the Washington, D.C. metropolitan area—all regions with high housing costs, limited land supply, and restrictive land-use regulations.

Closely related policies are statewide fair share laws, which require all local jurisdictions to make some contribution to the state’s overall affordable housing supply. California, Massachusetts, and New Jersey all have fair share laws, although the design varies across these states. New Jersey’s Mount Laurel Doctrine is the oldest and best known; after a series of lawsuits, the state Supreme Court ruled that all municipalities have an “affirmative obligation” to allow housing development that would be affordable to low- and moderate-income families (Massey et al., 2013). In Massachusetts, Chapter 40B allows for the state to overrule local zoning and grant developers permission for housing projects that contain a minimum affordable share, if the community does not currently meet affordability criteria. California’s law requires local governments to grant developers a density bonus for any project with a minimum share of affordable housing (Schuetz, Meltzer, and Been, 2009). Both the New Jersey and Massachusetts laws are frequently invoked by developers seeking

**Exhibit 1**

**Summary of Local Affordable Housing Policies**

<b>Policy</b>	<b>Examples (adoption years)</b>	<b>Sources</b>
<b>Zoning/planning requirement</b>		
Inclusionary zoning	Washington, D.C. metropolitan area: Four counties, three cities and the District of Columbia (1974–2006)	Destorel Brown (2001); Schuetz, Meltzer, and Been (2009)
	Massachusetts: 99 cities and towns (1972–2004)	Schuetz, Meltzer, and Been (2011, 2009)
	New York: New York City (1987)	Furman Center (2012)
	San Francisco Bay Area: 55 cities and counties (1973–2006)	Knaap, Bento, and Lowe (2008); Schuetz, Meltzer, and Been (2011, 2009)
	Southern California: 17 cities in Los Angeles and Orange Counties (1983–2003)	Mukhija et al. (2010)
Statewide fair share laws	California: Mandatory density bonus (1979) New Jersey: Mount Laurel Doctrine (1975)	Schuetz, Meltzer, and Been (2009) Massey et al. (2013), State of New Jersey Department of Community Affairs (2011)
	Massachusetts: Chapter 40B (1969)	Koshgarian, Clayton-Matthews, and Bernstein (2010); Schuetz, Meltzer, and Been (2009)
International parallels	United Kingdom: Town and Country Planning Act (1990)	Austin, Gurrán, and Whitehead (2013); Gurrán and Whitehead (2011)
	Australia and New Zealand: Local inclusionary zoning (2000–2008)	Austin, Gurrán, and Whitehead (2013); Gurrán and Whitehead (2011)
<b>Local financing mechanisms</b>		
Property tax abatement	New York City 421a (1971)	Ellen and O’Flaherty (2013)
Tax increment financing	California Community Redevelopment Agencies (1952)	Blount et al. (2014)
Shared equity homeownership	Community land trusts, limited equity co-ops	Temkin, Theodos, and Price (2013)

to build higher-density housing in wealthy suburban areas, although these efforts often face fierce resistance from local governments and residents (Fisher, 2007; Fisher and Marantz, 2014; Massey et al., 2013). By contrast, it is unclear how often California’s mandatory density bonus is used, apart from the local IZ programs.

Several zoning- or planning-based affordable housing programs are also in operation outside the United States (Austin, Gurrán, and Whitehead, 2013; Gurrán and Whitehead, 2011). In the United Kingdom, local planning authorities (similar to U.S. Zoning Boards) have widespread authority over nearly all new development proposals. Under Section 106 of the Town and Country Planning Act (1990), local authorities can choose to make development permission conditional on set-asides for affordable housing or other infrastructure contributions. The contributions are negotiated on a

case-by-case basis. Several local governments in Australia have adopted some version of IZ during the past decade, generally granting density bonuses in exchange for affordable housing. In 2006, South Australia adopted a broader IZ policy that takes effect with rezoning requests. New Zealand also has some local IZ programs. The Affordable Housing Enabling Territorial Authorities Act of 2008 grants local councils the right to require affordable housing from private developers with no subsidy.

One of the reasons why IZ and related policies have become popular is that they shift the cost burden for developing affordable housing onto private developers (and through them, to market-rate renters and homeowners or to land owners).<sup>2</sup> That is, local governments and existing community residents face no direct fiscal costs to produce affordable units. However, a few states and localities have adopted local financing mechanisms that are specifically earmarked to subsidize affordable housing development. Although these earmarks are fairly rare, the mechanisms offer some insights into possible program design.

Tax increment financing (TIF) is frequently used to generate local revenues that can be targeted to particular geographic areas and purposes. TIFs are widely used in commercial areas for economic development and for infrastructure financing (Immergluck, 2009; Smith, 2009). The most widespread application of TIFs for affordable housing was in California through the state-established local community redevelopment agencies (CRAs). Through the CRAs, cities and counties could designate “blighted” urban areas in need of redevelopment, which allowed for them to retain the growth in property tax revenue from those designated areas to finance projects with public benefits, including affordable housing. From 1952 until the dissolution of the CRAs in 2011, projects financed through the CRAs were a substantial contribution to affordable housing development in California (Blount et al., 2014).

New York City’s 421a program offers property tax abatements to developers for newly constructed multifamily buildings in designated parts of the city (Ellen and O’Flaherty, 2013; Furman Center, 2016). The program is designed to encourage new development of rental apartments in lower-housing-cost areas (outside Manhattan and some high-priced outer borough neighborhoods, such as Brooklyn Heights and Park Slope). The standard property tax exemption lasts for 15 years, but developers can qualify for longer exemptions if they set aside 20 percent of the apartments for low- or moderate-income families.

Affordable housing created through local IZ programs, state “fair share” laws, TIFs or property tax abatements can in theory be either renter-occupied or owner-occupied, although in practice most programs focus on rental housing. A small number of localities have experimented with shared equity homeownership programs for lower-income households. These programs also take different forms, with the common element being some restrictions on resale prices, so that the units remain affordable to future homebuyers (Temkin, Theodos, and Price, 2013; Voith and Wachter, 2012).

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<sup>2</sup> Who ultimately bears the tax imposed by IZ (and similar policies such as impact fees) is a matter of theoretical and empirical debate. In general, tax incidence will depend on the relative elasticities of supply and demand for housing but can also be affected by program design features such as the presence and size of cost offsets (density bonuses). Moreover, whether affordable housing is considered an amenity or disamenity to the nearby property owners can affect land values. See Huguen and Read (2013) for a formal model of IZ, or Ihlanfeldt and Burge (2006) and Burge (2014) for discussions of impact fees.

Examples include Community Land Trusts, under which qualified buyers purchase the house but land ownership is retained by the trust, Limited Equity Cooperatives, and deed-restricted homes. All these programs require some upfront subsidy for the initial purchase or development of houses, but in theory the programs can then be self-sustaining as houses cycle through purchase by income-qualified buyers.

Equally important as producing new affordable housing is the challenge of preserving the existing affordable stock, both subsidized and unsubsidized. The inventory of low-cost housing can be eroded in several different ways, each of which has slightly different policy implications for preservation. An extensive literature has documented the problem of expiring affordability restrictions from subsidy programs such as LIHTC, HUD-subsidized loans, IZ programs and New York City's 421a tax abatement (Lens and Reina, 2016; Schwarz et al., 2016). Because all these programs are initially applied for a defined time period, once that period ends, landlords have an incentive to remove the affordability restrictions and raise rents to market levels—particularly if housing markets are strong and the property is in a desirable location. Research has shown that maintaining affordability after subsidies expire generally requires additional funds from public agencies, philanthropies, or specialized financial intermediaries (Schwartz et al., 2016).

Unsubsidized low-cost housing is also in danger of exiting the affordable inventory through both upward and downward filtering. During the past 20 years, housing prices in many markets have increased faster than incomes for low- and moderate-income households, so that many initially affordable units are no longer within reach for low-income households, absent vouchers or other household-based subsidies (Howell, 2013). Alternatively, landlords sometimes neglect maintenance on low-rent units, which can deteriorate physically until they are no longer safely habitable. Ironically, the inventory of low-cost unsubsidized units depends in part on weak enforcement of building code and health standards by local government agencies (Desmond, 2015). Whereas filtering is typically a gradual process by which relatively small shares of units exit the affordable housing inventory each year, negative shocks can remove large numbers of units simultaneously; for instance, a local government's decision to close a mobile home park or fire damage to a large apartment building. In some instances, then, local governments may choose to work with landlords to bring properties up to code or assist with resident relocation.

## **How Much Affordable Housing Have Local and State Policies Produced?**

Both policymakers and housing researchers are interested in understanding how effective these state and local programs are at producing and preserving affordable housing. How many affordable units do the various programs create? How does production vary within jurisdictions over time, either because of housing market conditions or changes to the program's design and implementation? Can different programs in similar locations—or similar programs in different locations—be compared to learn what design features work best with certain housing market characteristics, or when combined with other public policies?

Unfortunately, empirical research on these questions has been very limited, because many state and local governments that oversee affordable housing programs do not maintain consistent records

on output. Mukhija et al. (2010) described the difficulties of collecting even basic information from multiple local governments and then trying to shape the raw numbers into data that can be consistently analyzed (for instance, some local IZ programs that allow for in-lieu contributions do not track whether those contributions have produced affordable units off site or at a later date). In an environment that increasingly stresses “evidence-based policymaking,” the lack of timely, consistent, reliable data on even basic program elements and output is a serious barrier not only to academic research but to governments’ own ability to assess the effectiveness of their policies.

To analyze the efficacy of local IZ programs and statewide policies in California, Massachusetts, and New Jersey, we assembled data on affordable housing production from several existing studies (exhibit 2). It is difficult to make apples-to-apples comparisons, because most studies report snapshots of production for a limited set of geographies at one point in time, but the underlying programs were adopted (and revised or rescinded) over several decades. Because both local IZ and statewide programs rely on strong demand for market-rate housing to finance affordable units, we would expect to see large variations in the annual output of these programs during housing market cycles. To provide some comparability, we have calculated average annual affordable housing production for more than 150 local IZ programs across five regions of the country. These regions were chosen for data availability, but they also represent some of the oldest, most widely studied programs. Not coincidentally, they have also historically had some of the highest housing costs—and most severe affordability problems—in the nation. To give some context for the scale of housing produced under local IZ programs, we also present the average annual number of LIHTC units built in the same jurisdictions during the same time periods, and the total housing stock.<sup>3</sup> More details on data sources and calculations are provided in the notes to exhibit 2.

Average annual production under local IZ programs varies systematically across regions, but in all areas has contributed only a modest amount of affordable housing. The highest production levels

## Exhibit 2

### Comparing Affordable Housing Production From Local IZ Programs

	IZ Programs	Average IZ per Year	Average LIHTC per Year	Total Housing
Northern California	55	14.9	46.8	23,186
Southern California	17	31.7	41.5	34,762
Boston suburbs	99	1.8	9.6	9,349
Washington, D.C. suburbs	4	220.4	269.2	264,645
New York City	1	178.5	4,499.7	3,200,912

*IZ = Inclusionary Zoning. LIHTC = Low-Income Housing Tax Credit.*

*Notes: Data on northern California IZ, Boston suburbs, and Washington, D.C. suburbs come from Schuetz, Meltzer, and Been (2009). For those regions, IZ production totals were observed from 2004 through 2006. Data on IZ in southern California are taken from table 5 in Mukhija et al. (2010), which reported production totals through the summer of 2006. Estimated IZ production for New York City comes from Furman Center (2016) and reflects the maximum reported in the estimate range (4,999 units). Average IZ units per year are calculated for each jurisdiction, using the year IZ was adopted through the most recent date affordable housing production is reported. Average LIHTC units per year are calculated for the same jurisdictions, matching the time period of IZ production as much as possible. LIHTC units are taken from the U.S. Department of Housing and Urban Development public database. Total housing counts are taken from the 2000 decennial census.*

<sup>3</sup> Several other papers in the IZ literature use LIHTC production as a benchmark for assessing production levels; Mukhija et al. (2010) discussed strengths and weaknesses of this approach. LIHTC has been by far the largest affordable housing finance source in the United States during the past 30 years, and granular data on production are readily available.

are found in the four Washington, D.C.-area counties and New York City. Notably, these jurisdictions are also the largest (most populous). Most of the IZ programs in northern and southern California are in smaller suburban areas, and the Boston-area IZ jurisdictions are small towns. Jurisdiction size matters not only for housing demand, but for capacity of the local government. For instance, many of the Boston-area towns with IZ do not have full-time town managers or planning staff, whereas New York City and the D.C.-area counties have entire departments dedicated to housing, planning, and community development activities. Staff capacity may influence localities' ability to work effectively with developers and households in implementing the requirements of IZ, as well as to collect data on outcomes. In all the regions, IZ produces on average fewer affordable units than LIHTC, although this pattern is reversed within some individual jurisdictions. Expressed as a share of the existing housing stock, affordable housing produced under IZ is less than 0.1 percent of existing housing in all regions. For another point of comparison, New York City's 421a tax abatement program has produced on average more than 2,100 affordable units per year, more than 10 times the annual output of New York City's IZ program (Ellen and O'Flaherty, 2013).

Exhibit 3 shows equivalent statistics for affordable housing produced under the three largest statewide programs, which are in California, Massachusetts, and New Jersey. Once again the numbers are average annual production numbers, although two of the three reflect a limited period in the program's history rather than lifetime totals. As with local programs, output under the state programs is a tiny share of the existing housing stock, so is unlikely to substantially alleviate the need for affordable housing. In California and Massachusetts, the statewide programs have produced many fewer affordable units than LIHTC, although the statewide comparisons are less informative than at the local level.<sup>4</sup> The statewide averages may also obscure substantial variation in production levels across individual jurisdictions within each state; unfortunately neither California nor Massachusetts provide local data on program output.

**Exhibit 3**

**Comparing Affordable Housing Production From Statewide Programs**

	Affordable Units per Year	LIHTC Units per Year	Total Housing
California (CRAs)	9,000	16,329	13,680,081
Massachusetts (Chapter 40B)	810	1,902	2,808,254
New Jersey (Mount Laurel)	1,673	380	3,553,562

*CRAs = Community Redevelopment Agencies. LIHTC = Low-Income Housing Tax Credit. Notes: Data on affordable housing financed by California's CRAs from 2001 to 2008 come from Blount et al. (2014). The count of affordable units produced under Massachusetts Chapter 40B from 2000 to 2010 is taken from Koshgarian, Clayton-Matthews, and Bernstein (2010). Completed construction of affordable units under New Jersey's Mount Laurel program is reported by State of New Jersey Department of Community Affairs (2011). Average affordable units per year are calculated for each state. For California and Massachusetts, production is calculated for the period reported in the underlying source. For New Jersey, production reflects the entire life of the program (1975 to 2011). Average LIHTC production is calculated for the same period as the statewide program (for New Jersey, average LIHTC production is calculated since 1987). LIHTC data are taken from the U.S. Department of Housing and Urban Development public database. Total housing counts are taken from the 2010 decennial census. LIHTC funds may be used to finance qualifying projects under all three statewide programs, so the counts are not necessarily mutually exclusive.*

<sup>4</sup> For instance, all the statewide programs apply only in certain designated areas—"blighted" areas in California and localities with limited affordable housing in Massachusetts and New Jersey. Tax credits can also be used in conjunction with all three state programs, so the totals are not mutually exclusive.

Investigating why local IZ and statewide fair share programs has been more effective in some localities and states is a crucial area for future research. A few studies have noted that mandatory IZ programs tend to produce more affordable units than voluntary ones, and that early adopter programs have built more units, even adjusting for time (Mukhija et al., 2010; Schuetz, Meltzer, and Been, 2009). However, these studies did not account for possible endogeneity in program design; jurisdictions that strongly favor affordable housing are likely to adopt IZ sooner and make it mandatory, but these same localities might have encouraged more development even with other types of programs. Besides housing market conditions and program design features, understanding the political support of local governments and local residents is important, particularly given that these programs are often adopted by localities with traditionally “exclusionary” zoning where existing homeowners may have ambivalent sentiments about introducing low-cost housing nearby.

## **Spillover Impacts on Surrounding Housing Markets**

The primary focus of this article is on the relative efficacy of state and local programs to produce affordable housing. However, it should be noted that all these programs have the potential to have broader spillover effects on state and local housing markets. Existing research has found mixed results of local IZ programs, with some evidence that IZ contributes to higher housing prices, reduced construction, and a shift toward smaller housing units, but these effects vary across regions and time periods (Knaap, Bento, and Lowe, 2008; Mukhija et al., 2010; Schuetz, Meltzer, and Been, 2011). Massey et al. (2013) documented the extended resistance by Mount Laurel and other wealthy townships to allowing for any affordable housing within their borders; 30 years of lawsuits, appeals, and countersuits have imposed high costs on both local governments and developers, not to mention generating political bitterness on both sides. Mitchell (2004) noted that, despite Mount Laurel, new housing developed in New Jersey is less likely to be in affordable structures. Some researchers have credited Chapter 40B with increasing the amount of higher-density, market-rate rental housing in many Massachusetts communities, because the law enables developers to bypass highly restrictive local zoning (Fisher and Marantz, 2014; Koshgarian, Clayton-Matthews, and Bernstein, 2010). Evidence on the broader effects of California’s CRAs is also mixed; Fauria and Mathur (2012) found positive spillovers of redevelopment projects on housing prices in Oakland, but Swenson (2015) concluded that CRAs have had minimal economic development benefits on CRA areas throughout the state. In general, both local IZ programs and statewide fair share laws are likely to have fewer distortionary effects on housing markets than earlier local policies aimed at preserving affordability, such as rent regulation (for instance, Autor, Palmer, and Pathak, 2014).

## **Conclusion and Policy Recommendations**

Rising housing costs strain the financial well-being of low- and moderate-income households in many U.S. cities. Building and preserving affordable housing is a challenging task. Increased demand for central cities by high-income households, together with limited land availability and complex development regulations, contribute to higher-market-rate housing costs. During the past quarter-century, wages for low- and moderate-income families have stagnated, while federal

subsidies for affordable housing and other social safety net programs have declined. Maintaining and increasing the supply of low-cost housing will require sustained effort from federal, state, and local governments, as well as nonprofit organizations. States and localities have pioneered a number of different policies to directly provide, or incentivize private developers to provide, affordable housing. The most common ones are statewide “fair share” laws and local IZ programs, although some localities also have designated funding streams through tax abatements or direct budget allocations. Unfortunately, most state and local programs have produced relatively small numbers of affordable units, and so are unlikely to substantially meet the demand for below-market-rate housing. Moreover, low-cost housing tends to be built where land is cheap and political opposition is muted, which in practice limits the ability of low-income families to move into neighborhoods with more employment opportunities, better schools, lower crime, and higher-quality public and private services. In this section, we outline several action items for policymakers, based on research findings.

A better understanding is needed of why existing state and local programs have produced only modest amounts of affordable housing and whether these programs could be redesigned to be more productive. Better data on output are therefore essential. State governments, affordable housing advocacy and research organizations could be useful allies in collecting and disseminating data. Not only do they have more resources than many local governments, they could play a valuable role in standardizing data reporting. Prior research has focused mostly on how program design impacts output. Equally important is an understanding of the political dynamics of both local and state programs. How can government officials build support among local residents who may be skeptical of allowing for low-cost housing in their neighborhoods? Although many localities in New Jersey and Massachusetts continue to oppose state mandates, some local governments actively encourage and invite affordable housing development as an essential part of well-functioning housing and labor markets (Pendall, 2008; Voith and Wachter, 2012).

Cities and counties should systematically reduce the regulatory burdens of development, thereby reducing the costs of new housing (or at least slowing future price growth). Restrictive and complex land-use regulations have been shown to decrease the amount of new housing, particularly multifamily apartments, and increase housing costs (Glaeser, Schuetz, and Ward, 2006; Malpezzi, 1996; Pollakowski and Wachter, 1990; Quigley and Raphael, 2004; Schuetz, 2009). A new survey from the National Association of Home Builders estimates that costs associated with complying with federal, state, and local development regulations amount to 24 percent of new house prices (Emrath, 2016). Modifying or removing unnecessary regulations, making the development process more transparent and less uncertain would over time translate into lower prices and rents across the entire housing distribution (Furman, 2015; Glaeser and Gyourko, 2008). This approach would also benefit moderate- and middle-income households that are increasingly squeezed by housing costs.

Local governments should increase the densities allowed under zoning across the jurisdiction (upzone), making it possible to produce smaller, lower-cost housing units. For instance, some cities are debating making it easier to create accessory housing units (such as in-law apartments) in single-family areas; such a change has the potential to create more affordable units that are generally consistent with the scale and appearance of existing neighborhoods (Badger, 2016; Rosan and Susskind, 2007). Under the past two mayors, New York City has engaged in selective upzoning

of some neighborhoods, such as East Midtown and Greenpoint/Williamsburg, while simultaneously downzoning residential areas in the outer boroughs (Laskow, 2014). Concurrent with development of the Washington, D.C. Metro public transportation system, Arlington County, Virginia, substantially increased allowable densities around Metro stations, encouraging high-density apartments and commercial activity, while preserving lower-density, exclusively residential uses elsewhere in the county (Arlington County, 2012). Although transit-oriented developments have increasingly been built, to date no city has systematically upzoned large shares of land as a mechanism to promote affordability.

Some cities have adopted policies that can target low-income residents of gentrifying neighborhoods. One approach for targeting residents of gentrifying neighborhoods is to provide preferences in new affordable housing developments for residents of gentrifying neighborhoods. For example, the city of Portland recently adopted a program that gives preferences for affordable housing units being built in the North/Northeast neighborhood to residents who were displaced as a result of past redevelopment efforts (HUD, 2016c). Similarly, affordable housing developments in New York City's Inclusionary Housing program give a preference for admission for residents of the surrounding neighborhood. Such preference programs have the advantage of making it easier for low-income residents of the neighborhoods undergoing gentrification to remain in these neighborhoods and would perhaps make long-term residents less wary of gentrification.

Preference policies are not, however, without controversy. New York City is currently being sued in Federal court (*Janell Winfield, Tracey Stewart, and Shauna Noel v. City of New York*) on the grounds that this preference policy perpetuates existing segregation patterns. HUD also rejected a preference plan by the City of San Francisco that would have given preferences to residents of the surrounding neighborhood on the grounds that the program would have reinforced existing segregation patterns (Dineen, 2016). Given the twin goals of fostering affordability and avoiding the exacerbation of segregation that many local housing agencies will have, preference policies may make sense only in communities that are not highly segregated, in conjunction with other efforts to combat existing segregation patterns, or both. As of this writing, the circumstances under which preference plans are allowable, if any exist, is unclear.

The main focus of this article is on local and state policies that do not require federal subsidies or assistance. However, two new federal initiatives are aimed at expanding accessible locations for low-income households under existing subsidy programs. First, HUD has recently proposed altering the rules of the HCV Program, in order to make it possible for voucher holders to access higher-quality neighborhoods. Traditionally, the maximum allowable Fair Market Rent (FMR) under vouchers—which is based on metropolitan area rents—has been too low for most voucher recipients to live in high-quality neighborhoods, particularly in more expensive metropolitan areas. The rule change, known as Small Area Fair Market Rents (SAFMR), would allow for the maximum FMR to vary across ZIP Codes within metropolitan areas. HUD estimates the new rule would enable more voucher recipients to rent apartments in low-poverty, high-opportunity neighborhoods (Henneberger, 2016; HUD, 2016a). Collinson and Ganong (2013) studied a similar experiment in Dallas and found that ZIP Code-based FMRs lead to substantial improvements in the neighborhood quality of voucher holders. Specifically, households moved to neighborhoods with lower crime, poverty, and unemployment rates and with better schools.

Second, in 2015 HUD adopted a new rule called Affirmatively Furthering Fair Housing (AFFH), which requires HUD grantees to set goals for reducing racial segregation within the jurisdiction (HUD, 2015).

AFFH will apply to cities, counties, and other localities that receive funds through CDBG, HOME, and similar federal programs. Neither SAFMRs or AFFH entail additional federal subsidies; both are essentially changes in the rules that apply to existing subsidy programs that HUD believes will accomplish similar goals as local IZ programs and statewide fair share laws—namely, enabling low-income households to access housing in higher-opportunity neighborhoods. As these rules are implemented during the next several years, policymakers and researchers should observe them and collect appropriate data that will allow for a rigorous evaluation of their effectiveness.

In an ideal world, “solving” the affordable housing puzzle would both increase the supply of low-cost housing in high-quality neighborhoods and improve underlying conditions in existing low-income neighborhoods. The first will require increased public support—both financial and political—for developing high-density housing in affluent communities. Alternatively, housing vouchers or other income supports could enable low-income families to access the housing that already exists in those communities. Improving conditions in lower-value neighborhoods will also require sustained support from public, private, and nonprofit actors. Public and philanthropic agencies cannot provide enough capital to revitalize areas, but can serve as seed money and can offer some protection for long-term residents in gentrifying (or about to gentrify) neighborhoods. To supplement these efforts, local governments and nonprofits need to attract and leverage private capital while creating mechanisms to retain increased land values. Ultimately, creating and maintaining an economically diverse housing stock across communities is essential for well-functioning regional labor markets, and for the well-being of many families.

Finally, we conclude by noting that, although the provision of affordable housing is a necessary component of any economic transformation that aims to be inclusive, affordable housing alone is unlikely to enable disadvantaged households to take advantage of new economic opportunities. The results of the MTO demonstration, which found poor adults to experience little in the way of economic mobility after moving into low-poverty neighborhoods, underscore this point. Although the MTO experiment found children who moved while young witnessing benefits in terms of increased earnings and higher graduation rates, benefits for adults were limited to health and sense of safety and security (Briggs, Popkin, and Goering, 2010; Chetty, Hendren, and Katz, 2015). These latter benefits are not unimportant, but they do not translate easily into increased economic mobility.

Efforts that attempt to marry the need for affordable housing with other aspects of human development stand the greatest chance of not only enhancing housing affordability, but putting housing assistance recipients in a position to improve their economic standing. HUD’s Choice Neighborhoods Initiative is an example of an approach that attempts to combine affordable housing with other components of human development necessary for economic mobility. To this end, Choice Neighborhoods have three foci—housing, people, and neighborhoods. The housing focus entails replacing distressed public and assisted housing with higher-quality, mixed-income units. The people focus aims to improve educational outcomes for youths and provide social supports for their families. Finally, the neighborhood focus attempts to remove barriers that might inhibit investment (for example, crime) and improve amenities that enhance the quality of life in the neighborhood. Such efforts marry affordable housing initiative to human development where affordable housing can be an integral part of an inclusive economic transformation.

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