The California Housing Disaster, and What to Do About It

Trying to solve California's high housing prices with rent controls on new construction has been a catastrophic failure for California. Look at the awful results from the 2014-2022 RHNA Cycle: For the 2014-2022 RHNA Cycle, California housing prices rose from 50% higher than US housing prices to 76% higher than US prices. A State that does so many things right, has utterly failed at housing policy.

The RHNA Cycle is the centerpiece of California housing policy. "RHNA Cycle" stands for the "Regional Housing Needs Allocation" by which the State assigns an 8 year housing allocation to each city, with that city obligated to rezone for the specified number of housing units in designated price categories (very low income, low income, etc..).

In a May 10, 2023 op/ed in the East Bay Times, David Garcia and Bill Fulton from the respected Terner Center for Housing and Innovation applauded recent California housing legislation which forces local governments to approve more housing. I agree.

Garcia and Fulton bemoan that the housing reforms have failed to increase the number of new housing units beyond just over 100,000 homes annually. Unfortunately, other policies being applied by the State Housing and Community Development Dept. (State HCD) are the primary reason why housing supply is not increasing. State HCD has adopted policies which effectively force most California cities into imposing inclusionary rent controls (mandatory rent controls on new construction enforced by deed restrictions) on a portion of new housing construction.

Nothing in the State Housing Statutes requires cities to adopt rent controls on new housing construction. But, the State HCD housing regulations only consider housing "affordable" if it is deed restricted to remain affordable (i.e. rent controlled) usually in perpetuity. Affordable by design housing such as smaller units are not counted as "affordable" because new market rate units cannot be produced at rent levels which meet State HCD's rent criteria. So, cities are virtually forced to impose inclusionary rent controls in order to get their housing elements certified by State HCD.

For exclusionary cities, determined to suppress their housing supply, inclusionary rent controls are a triple winner:
First, the serious cost burden of providing inclusionary rent controlled units seriously *shrinks the supply of new market rate housing projects*, thus driving up market rate housing prices.
Second, an increase in the price level *increases the home equity of every home voter*, dollar for dollar.
Third, "*We adopted inclusionary zoning requirements*" is the *safe and acceptable answer to State HCD* and the public to prove a city is "working" to provide affordable housing.

These inclusionary rent controls load the entire cost of providing affordable housing on to the consumers of new housing. In a 2021 case study, I found that the rent subsidies required by a 15% inclusionary rent control mandate equate to a rent increase of $192 per month for each remaining market rate unit – a 7.15% rent increase. In other words, the rent subsidies are paid by higher rents on the remaining units. That higher cost of producing units embeds into the housing price level creating tremendous negative leverage: According to a study I did in the year 2000, for every dollar of rent subsidy created by the inclusionary rent controls, market rate consumers then pay $13 in higher housing costs. The further insidious impact of inclusionary rent controls is that most new housing projects become infeasible.

This dreadful flaw in California regulatory policy could be corrected administratively by State HCD, or by any city genuinely interested in increasing affordability, simply by allowing units to also be counted as “affordable” based on unit sizes, rather than just by rent levels. An inclusionary mandate to make 25% of new apartments 650 s.f. or less would not cost the developer a single penny in lost rent. Without rent controls, developers could and would produce smaller “affordable by design” units in vastly increased quantities, which would drive down the price of market rate housing.

To understand how housing prices can be brought within reach of the millennial generation, and see data cited above, read “***The 2014-2022 RHNA Cycle: A Catastrophic California Housing Policy Failure***” by me at the following link:
https://www.dropbox.com/sh/0e4d1b9d9vmefwd/AAAww5rX2DfYpJo2is0xV6Aqa?dl=0

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