



PAT BROWN INSTITUTE OF PUBLIC AFFAIRS

WHITHER HOUSING IN CALIFORNIA?

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We all know there is a housing crisis in California. A few statistics will remind us:

- California's homeownership rate is the second lowest in the nation (59%) and is 10 percentage points behind the national average. In June 2006, the median cost of a home was \$575,800. To qualify to purchase such a home, a household must earn at least \$127,950. At the same time, the median income for a family of four in the state is \$54,140. Only 14% of the state's residents can afford it (CAR, 2006).
- While the median home price has skyrocketed, the number of sales has recently been decreasing, down by 26% from June 2005. So far, the decrease in home sales has not translated into a price reduction, but it remains to be seen if this occurs later in the year (CAR, 2006).
- Forty-one percent of all Californians rent—and face the greatest affordability challenges. Quarterly figures released by RealFacts (2006) indicated that, for example, rents rose 9.1% in the last quarter alone in San Jose, 6.8% in LA-Orange County.
- California is second only to Massachusetts in the hourly wage needed to afford a two-bedroom apartment at fair market rent (FMR). A California, extremely low-income family earning \$16,242 or 30% of the state median income (and just over minimum wage) can afford rent of \$406/month, but the average statewide FMR is \$1,014 (HCD, 2006).
- According to the California Budget Project, 25% of all renters pay over half their income for rent, and 35% of all renters pay over a third of their income for housing (CA Budget Project, 2004)
- California has over 300,000 people living in our streets, almost one third of them in Los Angeles County (Housing California, 2006).
- California has not built housing to keep up with demand, particularly for multifamily use. Multifamily units accounted for only 25% of all new units in the 1990s, a drop of almost 70% from the decade before. Since 2000, the number has increased slightly, to 28% of all new units built (HCD, 2006).

What makes the housing crisis seem so intractable, and what are the policy options facing us that could ameliorate this tragedy?



Systemic Problems With Housing in California

California's housing problems were not always a crisis. A series of shifts in the state's economy and demographics, along with the unintended consequences of state and federal policy, contributed to today's morass.

Two major economic shifts fueled the fire of our housing crisis. First, in the 1980s and early 1990s, California's economy moved from a manufacturing base to a service base. Higher-paid, "middle-class" jobs in aerospace and defense left and were replaced by lower-paid ones in various service industries. These were often filled by the large influx of immigrants, primarily from Central America but also from Southeast Asia—many of whom were fleeing war or its aftermath. With less income, these newer residents had a harder time buying into the housing market, remaining renters for decades (Haddad, 2006). Second, a combination of the dot-com bust and low interest rates led to much higher speculative investment in real estate, pushing prices to new heights beyond what the normal market would offer.

During the same general time period, several policy shifts depressed housing production. First, in 1986, Congress passed tax legislation that removed the depreciation benefit from rental housing, causing many apartment owners to leave the sector for other investment opportunities. Second, over these same years, the impact of Proposition 13 slowly eroded the state coffers, causing the state legislature in 1992 to shift property taxes from local jurisdictions to the state and providing sales tax instead. This, in turn, has led to the "fiscalization of land use," a process by which municipalities site retail establishments instead of housing production to fund local services. The third policy shift was the closing of state hospitals and mental institutions with the promise of community-based care that never materialized—creating a new, and large, class of homeless individuals that could in no way afford housing.

What's a State to Do?

The question California leaders must address is whether to rise to the occasion and tackle the difficult problem of where and how to house our residents or ignore the issue and leave our crisis to future generations. The question is not simple, however, since it brings into conflict two deeply entrenched—and contradictory—American value systems. First of these is our entrenched view that individualism and competition give



the “winner” the right to the spoils of their victory, i.e., their property; this country has long resisted any community restraints on private landholding. The second is our American communitarianism, a sense of community-building that evolved separately. We believe that our individual welfare is connected to that of our neighbor; we relish barn raisings and respond without hesitation to help those in trouble. Clearly, the push-pull between these two values creates political—and policy—conflicts.

If we can work through these overriding conflicts, what policies might we can propose and implement to move us beyond our immediate housing crisis? Policy analysts and researchers provide us with a short list of primary goals for state and local housing policy (Katz & Turner, 2003; Davis, 2006). Our to-do list includes the following:

- Given that the housing market is clearly closed to a large number of our residents, we must increase the supply of nonmarket, nonspeculative housing.
- Where the market has produced incredible wealth, we must redistribute some of this wealth toward housing for those shut out of the market.
- Where we have existing low-income housing, we must preserve and protect it.

Our next question is how to turn these goals into workable policies. A list of options follows.

- **Increasing the supply of nonmarket housing.**
 - The immediate option is to pass Proposition 1-C. Proposition 1-C is one of four infrastructure bonds on the November 2006 ballot. Substantial funds were provided by the voters in 2002 for the production of housing—both rental and homeownership—throughout the State. These funds are virtually depleted and Proposition 1-C would supplement them for at least three to four more years.
 - The longer-term solution is a state trust fund. California is one of only 15 states without an operational trust fund. Even with the constraints of Proposition 13, California leadership must push for and support a stream of revenue for such a fund. The source should be spread as widely as possible to produce the least amount of individual payment and yet provide the largest amount of revenue (Policy Link, 2005).
 - Local housing bonds. Cities and counties should pass housing bonds with a majority vote instead of a two-thirds vote, thus allowing a majority of the residents to determine at least part of their own housing future.
- **Redistributing the wealth generated from hot housing markets.** We can redistribute some of the wealth generated by the housing boom through funding the state trust fund. But we can do more at the local level.
 - Put real consequences into the housing element law. Given the fiscal constraints imposed by Proposition 13 and subsequent legislation, local governments often loathe to encourage and site housing production. Only



the state can see that this occurs both through incentives to local jurisdictions that do build housing and significant consequences to those that don't. Improving the housing element law and passing either statewide inclusionary housing principles or encouraging locals to do so can provide housing choice to everyone, not just a few. It is important to note that the California State Department of Housing & Community Development (HCD) reported that cities with a certified housing element clearly approve more building permits, *particularly for multifamily units* (CA HCD, 2006).

- Density, density, density. Realtors talk about location, location, location. The housing future in California is one of density. The state can both mandate and incentivize increased density through legislation on such proposals as accessory dwelling units, by-right development, and even parking requirements. While increased density does not, in itself, constrain market prices or redistribute wealth, it provides more supply to meet the ever-growing demand. A note of caution is warranted, however, because density is intricately connected to transportation. California will not benefit from increased automotive density, but from housing density.
- **Renters and multifamily housing.** California residents are predominantly renters, yet tenants have little protection from the housing market.
 - Allow more local rent control. The passage of the 1996 Costa-Hawkins bill virtually eliminated the protection of rent control at the local level. We cannot protect the low-income housing we have, however, if we do not address how to constrain the rental market. Overturning the law and allowing local municipalities to institute vacancy control if they see it as a useful tool is one step forward. A short step would be loosening the law's restrictions to allow cities to update their local rent control ordinances to include buildings more recently constructed.
 - Improve the renter's tax credit. California has careened back and forth regarding a tax credit for renters that would complement the mortgage interest deduction for homeowners. The present renter's credit could be improved.
 - Condo conversion. Having apartments converted to condos reduces the amount of rental housing available. Moratoria and condo conversion fees are a way to protect this housing or, at least, provide funding for the production of replacement units.

Proposition 90

Another November ballot initiative may have a large impact on local land use authority. Proposition 90 (Protect Our Homes Act), funded primarily by Howard Rich of New York, is part of a national effort to limit eminent domain for economic development. While a serious discussion of eminent domain may be worthwhile, especially in California, Proposition 90 includes in it a much wider definition of *takings* that will have



serious ramifications. The language says that any local policy that “results in substantial loss to private property” may be challenged in court. This is broad enough to include almost any local land use decision. Policy makers must address both the inequities in the use of eminent domain and the positive role it can play as intervention in a housing market.

Conclusion

As noted, we in California—indeed the nation—have a long history of conflicting values that we deeply subscribe to and support. These include both a strong belief in the right of private property ownership with little government intervention as well as the conviction that we are a common people who have built a society that values compassion and interdependence. These two belief systems sometimes conflict, but determining the level of government intervention in the housing market is one place where the conflict is front and center. No one policy completely reconciles these systems, and each policy initiative will lean more toward one or the other. However, given the potential of the housing crisis’ long-term impact on residents, infrastructure, and—indeed—our whole economy, finding a way to implement communitarian values may be a necessity if we want to maintain our capitalist viability.

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