Peer Review:
Analyses of Housing Affordability in Arizona
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Prepared for:
League of Arizona
Cities and Towns

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Introduction

This peer review was completed by Rounds Consulting Group, Inc. (“RCG”) for the League of Arizona Cities and Towns (“League”). A peer review is an independent evaluation of a professional document by qualified individuals in the relevant field of study. In this case the field of study is economics with an emphasis on housing, public policy, and economic development.

Note: This peer review is meant to be based on factual information and unbiased research, and be independent of any individual, group, organization, or government entity’s goals and objectives.

Topic Background

Housing is a basic need that provides economic stability, affects health and well-being, and fosters social equity. Recent surges in housing costs and availability issues throughout the nation and in Arizona have led to housing affordability concerns.

Studying housing affordability and development constraints is critical because it can help shed light on the cause of the economic imbalances. The research can help identify inefficiencies, opportunities, and public policy solutions to correct the imbalances.

List of Peer Reviewed Studies

Several studies have been completed related to the state’s housing availability, affordability, and development concerns. Various policy recommendations have also been presented in the studies. This review includes an evaluation of:

- A report prepared by an out-of-state consulting firm for the Arizona State Legislature¹,
- A report prepared by a local think tank organization²,
- A number of analyses of housing development constraints prepared by a university research institute that specializes in public policy.³

These documents were reviewed for basic content and any policy recommendations were also assessed for viability and effectiveness.


³ Morrison Institute Housing Research: https://morrisoninstitute.asu.edu/content/morrison-institute-housing-research
Executive Summary

Synopsis: While the referenced reports were well written and identify issues that impact housing development in the state, the documents exclude references to the macroeconomic conditions that have been the primary influence of housing development constraints and price changes.

Thus, the reviewed research papers conclude that local policies have been the main driver behind the increases in home prices and that local restrictions have contributed to the housing shortage more than any other factor. However, a review of macroeconomic conditions was beyond the scope of work in each paper.

For example, and most importantly, the reports exclude any analysis of the economic factors that resulted from COVID-19 disruptions and the federal government’s policy actions to mitigate the impact of the pandemic. These economic factors include widespread disruptions to the national and global supply chain, increases in the cost to transport materials, a lack of skilled and affordable labor, heightened federal government spending, and inefficient Federal Reserve Board actions. These influences continue to have an impact.

There was also limited reference in the reviewed reports regarding the degree to which each listed economic factor contributed to the current imbalances in the housing market. The impact of these individual factors needs to be studied so that recommendations can be analyzed for viability, receive a risk assessment for unintended consequences, and then be queued for staged implementation. Instead, the reports primarily list a set of selective concerns and recommendations with limited review.

Several areas of concern are indeed properly documented. Therefore, there appears to be some validity to the hypothesis that local level policies have impacted housing development volume. The outstanding question is, to what degree do local policies impact housing development.

Primary Report Exclusions and Areas of Excessive Focus

A number of major factors that were not considered in the reports that were reviewed relate to how macroeconomic issues have impacted housing development and affordability across the nation as a whole. It is assumed that this was beyond each of the report’s scope of work. A summary of key issues is included in Figure 1.

A primary factor that is excluded from consideration is the ongoing impact of COVID-19 policies and mitigation efforts as well as a change in socioeconomic patterns. The COVID-19 disruptions created various supply chain problems, including labor and material shortages, transportation delays, shifts in production, and higher commodity costs. This also led to a rise in remote work and a shift in housing preferences.

The federal government also overreacted with excessive and imperfectly directed stimulus spending, maintained interest rates at near-zero percent for too long, and released excessive money into the economy through bond buying. For some context, M2 money supply (i.e., a measure of the money supply that includes cash in circulation, checking deposits, and other types of deposits that are readily convertible
to cash such as savings accounts and CDs) increased by more than 40% in just two years, an unprecedented increase.

**Figure 1: Factors Impacting Housing Development and Affordability**

*Historically, the state has been more cyclical than most states in regard to housing. This is partially due to residential property taxes being comparatively low and the rate of population and employment growth being robust and consistent.*

Several community design standard documents for various municipalities going back as far as 2005 (pre-Great Recession) were examined to assess whether or not significant changes have been made to impact housing development. This review did not identify any changes in the standards that were consequential enough to create housing price inflation to the degree it was realized.

Historically, housing affordability was not a major concern in the state, implying that municipalities did not excessively restrict new development. When the excess housing construction occurred prior to the
Great Recession of 2008, the local communities in Arizona were not accused of being overly efficient with their development standards.

It is estimated that macroeconomic influences represent between 85% to 90% of the current housing availability and affordability issues while state, county, and municipal policies may have contributed to the remainder.

Instead, it is universally acknowledged that broader macroeconomic forces combined with unusual lending standards caused the over-development that partially led to the 2008 recession and weak economic recovery that followed.

This is not intended to diminish the fact that cities and towns have a responsibility to implement policies and strategies to help mitigate housing affordability issues throughout Arizona to the extent possible.

Several improvements can be made by local municipalities to allow for things like smaller lot sizes, additional housing units on the same lot, more efficient public reviews, more economical building design standards, and economic-based general plans and zoning designations.

RCG has been involved in the preparation of scores of analyses for developers in response to decisions by municipal governments to not move forward with proposed housing projects. In most cases, the economic evaluation demonstrated that the rationale for the initial project rejection was based on incomplete information and approval was later provided. In other cases, the developer’s plans were poorly designed and overreached beyond what was reasonably planned by the municipality.

This process should become more efficient in the future, but the implication that city and town specific practices had more than a marginal impact on housing price inflation and development volume post COVID-19 is inaccurate.

Finance and Economic Development Data Considerations

Between 2010 and 2022, according to the U.S. Bureau of Labor Statistics (“BLS”), the average percentage of household income spent on housing only increased from 33.6% to 34.3%, respectively. This is a very modest increase and implies that little harm to households has occurred. However, this does not tell the whole story. The percentage spent on housing varies significantly by income group.
The percentage of income spent on housing declines as income increases. In other words, higher income households spend a smaller portion of their total income on housing than lower income households.

Thus, housing affordability cannot be described using overall averages. Instead, housing supply and demand at each increment of household income must be calculated.

According to the BLS, households earning below $30,000 a year spent, on average, 41.2% of their income on housing. Those households earning between $30,000 and $49,999 spent 37.2% of their income on housing, while households earning between $50,000 and $99,999 spent 35.3% of their income on housing. The highest earning households, those earning over $100,000 a year, on average spent 30.8% of their income on housing. Thus, changes in housing costs disproportionality impact lower income individuals.

Regardless, the reviewed reports do provide a listing of certain municipal-level policies that have contributed to home price escalation at the margin. If these existing barriers are removed, the development of housing in the state could become more efficient, but the changes will not result in major shifts in the development of affordable housing or rectify the current imbalances if not combined with changes in macroeconomic policies.

Based on the completion of hundreds of economic analyses over the past two decades related to construction within Arizona, it is estimated that the legislature’s identified “inefficiencies” in municipal government practices contributed no more than 10% to 15% to the current price levels. An even smaller percentage relates to the recent price escalation. Most of the impacts are already imbedded in the historical baseline.
Select Recommendations and Findings – Municipal Polices

In an attempt to address the listed housing availability and affordability issues, various techniques, tools, and recommendations have been identified such as waived permitting and development fees for low-income housing projects and focused tax incentives, among others. Several constraints to housing development have also been identified; among these are macroeconomic factors, government restrictions, and community resistance to new housing development.

State policymakers will not be able to impact the broader macroeconomic conditions that have resulted in the current housing affordability crisis. Local policy changes can, however, marginally impact housing affordability and allow for additional housing units to be constructed.

This is not a “fix” to the housing crisis, but it does move the state closer to having a more efficient process so that residents can benefit from an affordable market. Several areas of improvement can, and should, be considered at the municipal levels of government such as:

1. **Economic Based Rezoning**: Cities and towns place too much weight on current land use plans and zoning designations that were developed with limited economic analysis. Land use plans are simply guides for how a community could develop. Cities and towns should review their land use plans (and zoning designations) more regularly. Waiting for a General Plan update to address these issues is inefficient.

2. **Public Input Limitations**: Policymakers at the municipal level need to utilize fact-based research to identify what makes for efficient development patterns, and only consider public feedback as a secondary input into the development approval process.

   It has been observed on multiple occasions that a very small number of local residents (with almost no economic facts in their possession) can derail a well-considered development proposal. Resident input should be considered as qualitative rather than quantitative, and be a part of the decision-making process but not the primary part. This will require local policymakers to rely more on economic analysis and less on NIMBY (“not in my back yard”) positions.

3. **Design Standards**: City and town approved building and site design standards are not the reason why price escalation occurred in the housing market. These standards have always existed to some degree. However, the review of historical design standards did identify areas of questionable regulation. It appears that the design standards can be separated into three components.

   First, select requirements may be a matter of safety, such as restrictions on side entry main doors. However, the location of a main entry door is often designed based on the configuration of the lot and cost needs to be weighed against more thoroughly researched safety concerns.

   Second, select design standards may be based on maintaining continuity between subdivisions. If done well, this could help to address NIMBY issues. If done poorly, it will result in an unnecessary cost.
Last, some design standards are based on personal preference of city/town staff and policymakers, and are an unnecessary requirement for developers to follow. Roof pitch is an issue in cold or wet weather climates, but it is not as relevant in moderate and hot climates. Color palette requirements may or may not be reasonable for a city or town to impose. However, these issues need to be initially dealt with at the municipal level.

4. **Other Restrictions:** It has also been observed that improved discussions are needed in determining lot sizes, allowing multiple dwellings on a single lot, and parking requirements, among others. *Also keep in mind that property owner rights need to be considered when a municipality imposes development restrictions.*

5. **No Cost Tax Policy:** There may exist opportunities to improve a community’s housing affordability while also improving the community’s economic development prospects.

For example, residential infill projects at vacant or blighted commercial sites are often too costly to redevelop, so it is difficult to lure a housing developer to clear the site and construct a residential development. One proposal is to freeze the municipal property tax payments at the current level (i.e., the lower value of the vacant/blighted buildings) and apply the fixed tax obligation over a set period of time as an incentive for the infill developer to make a normal profit.

Furthermore, techniques to fund local infrastructure such as value capture should be examined in more detail. Value capture is a type of public financing tool, such as tax incremental financing (“TIF”), that allows local governments to capture additional tax revenues as a result of increased property values.
Developer Responsibilities

What was not presented in the reviewed reports is the fact that developers can also complicate the rezoning process or be unreasonable when it comes to changes in zoning. If a developer purchases land that is designated for industrial use, for example, rezoning to residential use is not guaranteed.

In this example, the developer purchased the land that needs to be rezoned for their proposed residential project at a discount and, therefore, it is not unreasonable for the developers to bear the risk of the project not being approved. Furthermore, while a zoning change for a developer may result in higher profits for the owners, it may result in weakening a city or town’s economic position.

While it is a municipality’s responsibility to make sure that development restrictions and designations are based on analysis and not personal preferences, it is the developer’s responsibility to demonstrate that a zoning change makes economic sense to the community. In these cases, the review process may take longer than projects where changes in zoning are not required.

Typically, homebuilders do not complete a full evaluation of a city or town’s economic development plan and construction pipeline; thus, they cannot definitively indicate that a project refusal is not in the best interest of the overall community.
Process Conclusions & Observations

Substantial analysis gaps were identified in the documents that were reviewed. Therefore, it would be irresponsible to make permanent public policy changes to municipal level decision-making without gathering additional information and considering any potential unintended consequences. However, improvements do need to be made. Suggestions are included in the body of this report for policymakers to consider.

There are various housing affordability issues impacting different groups of people throughout the state, and future proposals should be focused on the varying type of need. One should consider that the housing needs of low-income individuals (those with disabilities, earning minimum wages, etc.) are different than the needs of typical “workforce” families (i.e., entry-level professionals, firefighters, teachers, healthcare workers, etc.) and that of middle- and upper middle-class households.

Proposals can be implemented in each of the various classes of housing that will partially advance affordability conditions in the state until the broader macroeconomic influences are reduced in scale of impact. In the cases when external economic factors are temporarily impacting local economies, it is dangerous to implement permanent changes to state law. This is also considered to be an inefficient approach to public policy.

Under current conditions, expectations should be reasonable as should changes to state regulations. The overall housing affordability problem in Arizona will not be resolved through the full set of recommendations contained in the reviewed reports without also imposing some degree of damage to the economy.

*This is a clear case of quality work being completed, but the depth of review being insufficient to warrant the regulatory proposals being considered.*

*Policymakers that truly want to improve the state’s economy should have no problem with embracing the fact that additional discussion and collaboration is needed between the state’s cities and development community.*
Economic Factors & Housing Affordability

The current housing affordability issues in Arizona were caused by several economic factors, most of which are due to the ongoing impact from the COVID-19 pandemic and the federal government’s response. This, coupled with demand and supply imbalance, resulted in an increase in housing prices and rents, making it challenging for some Arizonans to afford adequate housing.

The COVID-19 Recession

The COVID-19 pandemic led to temporary business closures and supply chain issues, and the federal government’s response (which included excessive stimulus spending and prolonged near-zero interest rates) contributed to inflationary pressures and increased investor activity in the housing market.

There are several problems with how the federal government responded to the crisis. First, the COVID-19 recession impacted households very differently. Those with lower incomes (i.e., those making less than $40,000/year) had nearly a 25% chance of losing their job while those making over $100,000/year had a 5% chance of becoming unemployed. See Figure 2.

Figure 2: COVID-19 Impact by Income Group
Percent Change in Employment from January 2020 by Income Group

The government also anticipated the recession would be lengthy, much like the Great Recession of 2008 (similar to the red dashed line in Figure 3). This led to a reaction by federal policymakers that included an excessive amount of fiscal stimulus that was poorly targeted and implemented. However, the COVID-19 recession was much shorter in duration (see the solid red line in Figure 3).
These fiscal impacts were exacerbated by Federal Reserve Board actions that included a policy of near-zero percent interest rates for an extended period of time coupled with an excessive increase in money being inserted into the economy. See Figures 4 and 5.

**Figure 4: U.S. Federal Funds Rate**
Average Monthly Effective Rate Since 2000

Note: Grey bars depict recession periods.
Source: Board of Governors of the Federal Reserve
The cumulative result was an economy that was realizing a significant amount of money to access at a very low cost, regardless of whether or not a household or business was in need of the government’s assistance. If a household made more than $100,000 per year, on average, it net-benefited financially from the COVID-19 recession.

Financing was readily available for real estate investors and households wanting to upgrade their housing or purchase a secondary home. This pushed housing prices to levels that are considered unaffordable to middle- and lower-income residents. However, the pattern of housing affordability being more cyclical in Arizona versus the remainder of the country has always existed. See Figure 6.

Figure 5: U.S. Money Supply
Average Monthly M2 Money Stock (i.e., Money in Circulation) in Billions

Figure 6: Median Sales Price of Homes Sold in Arizona & the U.S.
While the financial situation certainly contributed to higher housing prices, the extent of the labor and materials shortages, and tangential cost increases, eventually made it financially difficult to construct lower priced housing.

This is an important point. There are various housing affordability issues impacting different groups of people throughout the state, and future proposals should be focused on the varying type of need.

One should consider that the housing needs of low-income individuals (those with disabilities, earning minimum wages, etc.) is different than the need of typical “workforce” families (i.e., entry-level professionals, firefighters, teachers, healthcare workers, etc.) and that of middle- and upper middle-class households.

To simplify, the provision of affordable housing can be reduced to the following three product types:

- **Low-Income Housing** projects will not be built without government subsidies, even under the most favorable economic conditions. This is a financial fact that will not change with additional state regulations or progression through the current business cycle. Housing for low-income households will require property tax breaks (especially for redevelopment projects), Low-Income Housing Tax Credits ("LIHTC"), vouchers, or other forms of subsidies. Local municipalities also have a tendency to avoid such projects and some degree of policy reform is required for this type of housing.

- **Workforce Housing** projects (i.e., housing for entry-level professionals, firefighters, teachers, and healthcare workers, etc.) are rarely built when construction costs are unusually high (i.e., material/labor shortages, inflation, etc.) and if the cost of rezoning property is unfavorable. Negative responses from neighbors and the local community have caused various multi-family proposals to be abandoned, limiting the supply of workforce housing.

- **Market Rate Housing** development, including both single- and multi-family housing, has been limited compared to previous cycles. Limited new inventory combined with macroeconomic factors (such as low interest rates, excess stimulus, etc.) has caused home costs to further increase beyond the macroeconomic factors previously addressed, making homeownership less attainable to certain middle- and upper middle-class individuals.

Proposals can be implemented in each of the three listed classes of housing that will partially advance affordability conditions in the state until the broader macroeconomic influences are reduced in scale of impact. In the cases when external economic factors are temporarily impacting local economies, it is dangerous to implement permanent changes to state law. This is also considered to be an inefficient approach to public policy.
Peer Review - Housing Affordability Reports

Several studies have been completed in regard to Arizona’s housing affordability, availability, and development concerns. This review primarily focused on the following analyses:

- A report titled *Analysis of Housing Availability and Affordability in Arizona with Policy Recommendations*\(^4\) prepared by Anderson Economic Group, LLC. for the Arizona State Legislature’s Housing Policy Study Committee.

- A report titled *Housing Innovation in Arizona: Opening the Door to Arizona’s Housing Future*\(^5\) that was prepared by Fellows at the Common Sense Institute, a research organization in Arizona.

- Various reports\(^6\) prepared by the Morrison Institute for Public Policy, a policy research institute of Arizona State University, regarding housing development barriers in Arizona.

The reports also included various public policy recommendations for consideration. The reports were reviewed for basic content and any policy recommendations were also assessed for viability and effectiveness.

**Review of the Anderson Economic Group Report**

The first report, titled *Analysis of Housing Availability and Affordability in Arizona with Policy Recommendations*, was prepared by Anderson Economic Group, LLC (“AEG”), a consulting firm based in East Lansing, Michigan. The report was prepared for the Arizona Legislature’s Housing Policy Study Committee and sponsored by The Arizona Association of REALTORS.

The report provides a historical summary of housing statistics in defined regions across the state and will prove to be a valuable resource as housing affordability policies are developed in the state during the next few years. However, the presented recommendations are not meant to be firm in that the report does not suggest how formally the observations need to be considered and what remedies are appropriate.

**Broader Observations – AEG Report**

Housing affordability in the AEG analysis is broadly defined as a household spending 33% or less of pre-tax income on shelter. In other words, a home dwelling is deemed affordable to its occupants if housing costs do not exceed 33% of the household’s income.

Any analysis with a finite scope of work will utilize specific data points to compare and contrast. However, using a single variable for defining “affordability” could give the impression that the resulting affordability


\(^6\) Morrison Institute Housing Research: [https://morrisoninstitute.asu.edu/content/morrison-institute-housing-research](https://morrisoninstitute.asu.edu/content/morrison-institute-housing-research)
statistics are also specific and finite. The 33% statistic is less important than the extent the actual data point has changed over time, and to what extent the change occurred for each income group.

Clearly the affordability of housing has declined, but an overall average of 34.3% of income spent on housing is modest and does not capture the underlying affordability problem. The primary issue is that current economic conditions will not allow the private sector to develop affordable housing for low-income households and certain middle-income (i.e., workforce) households and also earn a normal profit.

Review of Select Recommendations & Observations – AEG Report

The following points highlight AEG’s policy observations/recommendations that are the most relevant to the affordability discussion.

1. **AEG Observation: Arizona is short about 150,000 housing units.**

   **RCG Analysis:** This estimate is reasonably scaled compared to estimates from other organizations, but internal review identified a shortfall of between 40,000 and 80,000 housing units. Even with the state’s movement through the business cycle and reduced influence of macroeconomic factors that have put upward pressure on housing costs, it will take multiple years before supply and demand are back in balance, even at shortfall of between 40,000 to 80,000 units.

   An issue to address is the evaluation of the construction pipeline. Numerous cities and towns will count the entire number of housing units in the production process (e.g., pre-submittal/pre-approval, approved, platted, etc.) as their construction pipeline. This is an incorrect assumption.

   Typically, as a residential project moves along the planning process (Note: the process may vary by city and town), it is first identified as a “pre-submittal/pre-approval” project and then is
eventually classified as an “approved” project when it has been approved for development by a city/town council or planning commission.

Once the project has been separated into parcels and recorded with the respective County Assessor’s Office, the partitioned housing units are categorized as “platted.” Finally, the platted units are categorized as “active” once construction begins within master planned communities, subdivisions, neighborhoods, etc.

A review of data published by the Maricopa Association of Governments (“MAG”) for several “construction pipeline” housing estimates for municipalities identified that the number of delivered units represented less than 5% of the total count in the pipeline in any given year. Therefore, estimates of the number of housing units that will be delivered in the near future, using this methodology, have been greatly overstated.

Also, the housing shortage estimates (from all sources) is based on a set of assumptions that can be reasonably modified to produce a different number. For example, using a long-term vacancy rate to identify current shortfalls in housing units does not account for changes in the state’s economy over time. The vacancy rate is simply a cushion that would normally accommodate imperfections in the housing supply and demand balance.

Using persons per household data to calculate a shortage can also have flaws. The number slightly changes over time and is based on other factors such as the density of an area and household formation rates. Therefore, it is difficult to identify how many persons per household is deemed to be detrimental to the well-being of a household.

The primary issue instead relates to how many units are demanded above supply at each income level. There is no significant shortage of higher income housing. However, there is a shortage of housing for lower- to middle-income households.

The exact number pertaining to the state’s housing shortage depends on several assumptions. The exact number is also irrelevant. Proposals to allow the private sector to develop more efficiently and not at the expense of current residents are needed under any supply shortfall estimate.

2. **AEG Recommendation: Eliminate prohibitions on multi-family development, remove excessive parking requirements, and allow for smaller lot sizes.**

   **RCG Analysis:** This is one of the more direct and efficient set of recommendations contained in the report. RCG has conducted dozens of analyses related to zoning requests throughout the state. In the majority of cases, the economic arguments were in support of additional multi-family development.

   However, politics and community push back often intervened and many zoning requests that were defensible were initially denied. An extended period of further review and community engagement was then required. This added to the developer’s costs and occasionally caused the developer to reconsider the envisioned project.
There appears to be misinformation among many municipal planning departments and the local community. The misconception is that a multi-family development will increase crime, worsen traffic, lower home values, and produce a fiscal harm to a community.

*In reality, for economic development to progress, there needs to exist a balance of housing for multiple types of workers, from higher-income manufacturing employees to lower wage retail workers. Cities and towns that over-regulate and work against an economic balance will eventually realize economic harm that will prove to be self-inflicted.*

**RCG Recommendation:** The League of Arizona Cities and Towns is well positioned to provide initial guidance on these subjects. It is recommended that cities and towns establish a more efficient and manageable approach to evaluating residential projects, both multi-family and single-family developments, similar to how studies are completed by consultants and zoning attorneys that provide support or opposition to new development requests.

It is also recommended that the parking requirements and lot size issues noted in the AEG report be considered.

3. **AEG Recommendation: Address Accessory Dwelling Units ("ADUs") and Short-Term Rentals ("STRs").**

**RCG Analysis:** Allowing additional housing units to be constructed on private property (such as a backyard studio to be rented) will not significantly impact the long-term affordability issues in the state, but municipalities should be encouraged to allow for more units to be constructed on a taxpayer’s private property when conditions warrant the development flexibility.

Imposing additional regulations related to short-term rentals needs to be considered carefully since STRs are a significant part of the state’s economy. Research completed by RCG in early 2022 identified that the vacation/tourism STR market contributes $6.6B in annual economic impact in Arizona, supports 75,500 jobs annually, and produces over $500M in annual tax revenues.

But, STRs have indeed put a strain on certain local housing markets. The impact also varies significantly by city so a single policy solution may not be the most efficient to implement.

**RCG Recommendation:** Encourage but do not legislatively mandate the approval of more ADUs. However, legislative action may eventually be required related to STRs. First, the state should add one full-time equivalent position at the Arizona Department of Revenue to manage STR taxes.

Also, cities may need to impose a modest tax or fee increase on STRs to allow for local management and response on housing issues. Any additional taxes need to be locally determined and imposed, but excessive taxation and/or regulations will negatively impact the tourism industry in the state.
4. **Other Items:** Additional recommendations in the AEG report include land banks and value capture tools such as tax increment financing. These topics are complicated, and taxpayers could be negatively impacted if the programs are designed inefficiently. These topics require further review.

*The recommendation to streamline the approval process is legitimate, but “streamlining the approval process” should not be confused with automatic approval. Each community has a unique economy and housing market.*

Also, development fee reductions will not be efficient if the fees are designed to cover infrastructure costs as intended. However, a review of development fees should be completed more often to determine if the fees are balanced. Reduced fees for low-income housing projects could also be considered.

Inclusionary zoning, or the requirement of affordable units to be included in housing development plans, is also recommended by AEG. If developers can simply pay a fee to bypass the requirement, it amounts to a tax increase which will not be favorable when it comes to building more affordable housing.

Also, it appears that cities and towns have not been as proactive as possible in addressing housing supply issues and often avoid multi-family proposals, particularly low-income housing projects. Some communities have even held functions to debate whether or not more apartments should be built in the area. For perspective, the answer is more often than not “yes.”

**RCG Recommendations:** Statewide housing issues are simply the aggregate of scores of local housing market issues. There is no single housing market in Arizona. Also, the housing need varies by individual and household incomes. *It will considerably disrupt the economy if a single state standard is implemented related to development approvals.*
Instead, cities and towns should follow a set of reasonable steps when projects are proposed. The League should work with municipalities to design a local standard but flexible approach to evaluating development projects.

**RCG Final Thoughts/Recommendations – AEG Report**

As an alternative to an excessive legislative regulatory action, a more formal and complete declaration backed by quantitative research should be designed for all mayors throughout the state to sign (and aggressively support) that identifies multiple areas in need of improvement as it relates to affordable housing.

Arguments will be made that we, meaning the state, cannot wait for 2024. People will not have to wait in this scenario. Community leaders will be pressed to immediately become more proactive in the development of more housing. Reporting requirements can be included as it related to cities and towns approving or denying projects. If the denials are legitimate, then the local government entities should have no concerns with this recommendation.

This progress can be tracked by requiring each municipality to submit select data points related to development proposals and approvals as recommended by AEG. This will allow state policymakers to continue to maintain reasonable levels of regulation in the state, and instead focus on the provision of tools that can be used to encourage private sector development projects.

**Review of Common Sense Institute Report**

The second report was produced by the Common Sense Institute (“CSI”) in Arizona and is titled: *Housing Innovation in Arizona – Opening the Door to Arizona’s Housing Future*. The report provides excellent historical perspective on a number of housing and economic data points.

Several recommendations in the CSI report are supported by an analysis of data from Phoenix and Houston. While the data appears to be correct, the implied conclusions need to be more carefully considered. The Phoenix metropolitan area is historically a more cyclical area when it comes to the national housing market.

Prior to the Great Recession in 2008, the state’s housing market was considered one of the most affordable in the country. In fact, housing affordability was promoted by the economic development community in the state up until the COVID-19 Recession.

RCG was not able to find any recent cases where local municipalities formally amended their housing planning strategies to a degree that would explain more than 10% to 15% of the affordability problem. This is further evidence that national (and global) factors caused the majority of the current issues related to affordability.

States with high growth potential and low property taxes typically display more cyclical housing market data. Arizona has extremely low residential property taxes while those in Texas are among the highest in the nation. Higher residential property taxes reduce investor profits limiting the amount of feasible investor rental properties.
For context, the following table summarizes the average residential property tax rate and latest median sales price of a single-family home in the top 10 states with the highest property tax rates.

<table>
<thead>
<tr>
<th>State Rank</th>
<th>Avg. Residential Property Tax Rate</th>
<th>Median Sales Price of a Single-Family Home</th>
</tr>
</thead>
<tbody>
<tr>
<td>#1 New Jersey</td>
<td>2.21%</td>
<td>$427,300</td>
</tr>
<tr>
<td>#2 Illinois</td>
<td>2.05%</td>
<td>$236,700</td>
</tr>
<tr>
<td>#3 New Hampshire</td>
<td>1.96%</td>
<td>$404,200</td>
</tr>
<tr>
<td>#4 Vermont</td>
<td>1.82%</td>
<td>$331,700</td>
</tr>
<tr>
<td>#5 Connecticut</td>
<td>1.76%</td>
<td>$336,600</td>
</tr>
<tr>
<td>#6 Texas</td>
<td>1.66%</td>
<td>$336,900</td>
</tr>
<tr>
<td>#7 Wisconsin</td>
<td>1.63%</td>
<td>$260,600</td>
</tr>
<tr>
<td>#8 Nebraska</td>
<td>1.61%</td>
<td>$265,000</td>
</tr>
<tr>
<td>#9 Ohio</td>
<td>1.58%</td>
<td>$203,800</td>
</tr>
<tr>
<td>#10 Iowa</td>
<td>1.50%</td>
<td>$206,400</td>
</tr>
<tr>
<td>#39 Arizona</td>
<td>0.65%</td>
<td>$406,200</td>
</tr>
</tbody>
</table>

Note: Average property tax rate for 2020; Median sales price of a single-family home as of February 2023.
Source: The Tax Foundation, Redfin

The problem is that any inefficiencies at the local levels of government are now receiving more attention and leaders in those communities need to commit to a more aggressive approach to housing development so that modest relief can be realized until the negative macroeconomic factors are dampened.

The following recommendations are included in the CSI report. Some recommendations are grouped by type. RCG notes on each item are included.

1. **CSI Recommendation: Expedite Zoning and Entitlement Processes/Streamlined Design Review.**

   **RCG Analysis:** A common complaint is that municipalities have different policies when it comes to the development process. This is because different communities have different attributes, economic opportunities, and constraints (e.g., land availability, landlocked by other communities, height restrictions due to nearby airports, landscapes, highway access, etc.).

   *In reality, the overall process for getting a project approved is not that different from city to city. The issue is that cities are not always internally consistent when it comes to individual projects and that politics (from staff, policymakers, and the public) sometimes interferes.*

   The same is true for the design review process, a topic also addressed in the CSI report. Municipalities will sometimes micromanage individual projects. This is a problem if done at a large scale.

   **RCG Recommendation:** RCG agrees that process and design guidelines should be drafted by cities to utilize and observe. However, statutory requirements related to statewide standards applied to local development should not be considered until city leadership has a chance to respond in this area.

   *Again, a statewide regulation related to housing development will cause significant economic problems and ignores the fact that different communities have different economies, landscapes, constraints, and attributes.*
2. **CSI Recommendation: Empower the State Department of Housing to Grade Local Processes.**

   **RCG Analysis:** The Arizona Department of Housing (“ADOH”) does not have the resources to provide a review and grade local housing processes. Instead, ADOH should be the recipient of data related to housing development (as recommended by AEG).

   However, care should be taken in interpreting the data since different communities will naturally display different development statistics.

3. **CSI Recommendation: Develop Universal Statewide Zoning Definitions.**

   **RCG Analysis:** A common set of zoning definitions will benefit both the cities and the state’s overall economy. This will not interfere with municipal autonomy as long as every type of development is clearly defined. However, a transition may be time consuming and costly in regard to reclassifying existing structures, zoning districts, etc.

4. **CSI Recommendation: Identify Reasonable Schedules for County and Municipal Reviews with Penalties for Failure to Perform.**

   **RCG Analysis:** This is another topic where the data that is reported could be misinterpreted. Not every project that stalls is due to municipal delays. Developers often have incompatible proposals with unrealistic expectations and communities might not have the resources to expedite the review process. A state drafted arbitrary schedule could cause economic harm. Cities should have the opportunity to offer an alternative approach.

5. **CSI Recommendation: Limit the Number of Plan and Design Reviews and Re-inspections Focused Solely on Life and Safety Issues.**

   **RCG Analysis:** This can be a complicated topic and a centrally approved process will not be able to account for all scenarios. But, this is an issue that needs to be addressed. Problems of this kind are due to a lack of experience at the city/town staff level.

   An alternative recommendation is for the League to establish a committee of mayors and key staff to provide standards for other mayors to agree to follow.

6. **CSI Recommendation: Remove Municipal Adoption of Building Codes and Allow the State Registrar of Contractors to Adopt Codes for the State.**

   Again, a statewide solution to an industry that is considered to be a “market of markets” may not work and unintended consequences should be reviewed prior to implementation.

7. **CSI Recommendation: Amend the State Statute on Inclusionary Zoning and Permit Cities and Counties to Allow Affordable Units if a Developer is Reimbursed for the Cost of the Subsidy.**
RCG Analysis: Additional research and local government feedback should be considered before reform in this area is implemented. Further information related to these recommendations is discussed in the review of the Morrison Institute reports.

RCG Final Thoughts/Recommendations – CSI Report

The CSI report was well considered and includes several items to further research. However, like the AEG report, there was no consideration for the primary macroeconomic factors that led to the price spikes in housing across the nation and in Arizona.

There was also no identification of potential unintended consequences of the proposals, and excessive weight was placed on specific developer complaints with no real counter arguments being formally or informally made.

Overall, the CSI report is convincing that another step in the review process must occur, but not enough scrutiny and review has occurred to warrant permanent changes in state regulatory actions related to housing development. At a minimum, this review and local cooperation is a multi-year process.

Review of Morrison Institute Reports

The Morrison Institute (“Morrison”) has produced a set of housing related reports and, like the others, was professionally written and includes many points to consider. The reports, also similar to the others, exclude from review some of the more important influencing factors related to housing affordability.
Therefore, the conclusions should only be considered as ideas worthy of further review. Select recommendations/policy solutions included in the Morrison reports follow:

1. **Inclusionary Zoning** requires housing development projects to contain a certain number of below market rate housing units for lower income households. However, Arizona currently prohibits the implementation of mandatory inclusionary zoning by local governments.

   A potential solution posed by the reports is to remove this restriction and allow local governments to implement mandatory inclusionary zoning while compensating developers for the development of any mandatory affordable units; a similar system has been put into practice in Florida.

   **RCG Analysis:** Consider a version of this recommendation pending additional review.

2. **Rent Controls** restrict the amount that can be charged for rent by a landlord. In Arizona, currently, rent control implementation is preempted unless the property is owned by a municipality or the state.

   While rent controls come with both pros and cons, there are potential policy options in this space. Some being government-subsidized rent, tax credits offsetting the total rent cost, or incentive programs to prevent landlords from increasing rent rates.

   **RCG Analysis:** Rent controls are not recommended but alternatives exist related to building and maintaining housing for low-income households.

3. **Short-Term Rentals** or properties only rented for a short amount of time decrease the supply of long-term housing in the housing market. Because Arizona currently preempts short-term rental controls, the report poses an elimination of the preemption to allow local governments to implement controls that best suit their region’s needs.

   Another policy solution brought up in the report is to implement an additional short-term rental tax and use those revenues to fund affordable housing development.

   **RCG Analysis:** Consider a version of this recommendation pending additional review.

4. **Tax Increment Financing ("TIF")** is a system by which a portion of property tax revenues from selected regions are utilized to subsidize development and construction in that particular area.

   Arizona is reported as the only state without the ability to create new TIF districts. The report proposes that the creation of new TIF districts should be reconsidered, keeping the necessity for management practices and increased oversight in these areas in mind.

   **RCG Analysis:** Consider a version of this recommendation pending additional review. Note: there may exist constitutional issues.

5. **Industrial Development Authorities ("IDAs")** are nonprofit corporations created by the government to specifically promote economic development with financing.
The report cites that Arizona currently allows IDAs to operate in certain counties but expanding the regions in which IDA’s can operate outside of heavily populated counties could be a potential solution. This would allow financing for housing development even in less-populated areas, thus, expanding the total affordable housing supply.

**RCG Analysis:** Consider a version of this recommendation pending additional review. Note: IDA’s have the ability to provide financing outside of urban areas, but the financial terms do not always allow for such financial backing in higher risk regions.

Overall, the Morrison Institute report supports many of the conclusions found in the other reviewed documents. But, similar to the other reports, additional and more detailed research is needed prior to implementing a formal statutory change or approval of new funding for the listed housing projects.
Conclusions and Recommendations

Overall, the peer reviewed reports were professionally written and identified a number of items related to development constraints and government inefficiencies that should be considered by municipal leadership.

However, all of the reviewed documents excluded several key economic issues related to what caused housing prices to escalate so rapidly. Therefore, the set of recommendations must be reevaluated since they were formed with incomplete information.

A proposed housing policy declaration and set of more quantitatively scored solutions should be drafted by the fall of 2023 and supported through obtaining feedback from various cities/towns and the development community and should more thoroughly cover items missing from the debate thus far.

The declaration and progress in municipal development policies should be transmitted to the Arizona Legislature and the Office of the Governor. If no progress is made during 2023 at the local levels of government in partnership with the development community, then policymakers at the state level can later intervene in 2024 but with more complete information related to defining the true problems.