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EXECUTIVE OFFICE FOR ADMINISTRATION AND FINANCE

Policy Report

Bringing Down the Barriers: Changing Housing Supply Dynamics in Massachusetts

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Executive Summary

Massachusetts has enjoyed remarkable economic success over the last several years. With that success, however, has come rising house prices and rents. The rising prices increase the housing cost of renters and prospective homeowners, make it difficult for people to live in the communities in which they grew up or currently work, and hurt the economic competitiveness of the state to the extent that businesses and employees choose to locate in states with lower housing costs. Massachusetts housing production has trailed national rates, even while price increases have led the nation.

What is different about the Massachusetts housing market and what can be done to address the problem? What makes Massachusetts different is not that we subsidize less housing than other states—we actually subsidize considerably more. Rather, the key difference is that the private sector here produces less housing to meet demand than it does in other parts of the country. The market supply does not respond adequately to rising prices. Some of the problem is unavoidable, due to natural limits on land. But many of the barriers are of our own making, including restrictive regulations and "not-in-my-backyard" local policies.

This housing report, along with its companion piece, "Moving Beyond Serving the Homeless to Preventing Homelessness," culminates work on these integrally related issues by an Executive Office for Administration and Finance task force formed at the direction of the Governor and Lieutenant Governor. This report examines housing trends and barriers to housing production and lays out a program of initiatives to remove unnecessary barriers to the development of housing affordable across a broad range of incomes.

Parameters of the Problem

Measurements indicate that rents are on the rise and that house prices are rising faster than in any other state. As of the end of the second quarter of 2000, the House Price Index[1] for Massachusetts was growing at an annual rate of 13.7%, about twice the national average.

Despite the price increases, there has not been an increase in the growth rate of Massachusetts' housing stock. In 1999, Massachusetts was 47th in the nation in number of building permits issued per capita. The shortage of land available for residential development combined with restrictions associated with building make it more difficult for suppliers in Massachusetts to respond to changes in demand for housing.

While growth rates for all types of housing have declined since the boom of the late 1980s, the change in multifamily housing starts is particularly striking. Massachusetts produces multifamily housing at about one third the per capita rate that the nation as a whole does. Multifamily developments play an important role in creating lower cost, lower priced housing while preserving open space.

Massachusetts residents have family, household, and per capita incomes well above the nation's. However, a significant portion of the state's relative income advantage is offset by the state's

[1] The House Price Index compiled by the Office of Federal Housing Enterprise Oversight, a modified version of the Case-Shiller repeat sales price index, measures the annual rate of price change for sales of the same houses, thereby isolating market effects from price changes caused by differences in the mix of houses sold.

high cost of living, the most significant distinguishing component of which is the high cost of housing. The median house price has grown faster than median household income, and rising rents have outpaced the incomes of renters at the lower end of the income scale.

Barriers to Housing Development

Government policies that restrict the amount of land available for development and the density at which it can be developed have a severe impact on the housing market. A detailed analysis of 16 communities in the Commonwealth by the Executive Office of Environmental Affairs indicates that the density allowed for new residential development by current zoning regulations is on average half of the existing residential density. According to Anthony Downs, an economist with the Brookings Institution, "the restrictive behavior of local governments—expressed through their various regulations—is by far the most important single cause of high housing costs."[2]

Local governments intervene in the housing market and restrict growth for many reasons. One is the fear that new housing may change the character of a city or town and generate increased traffic congestion and pollution, or alter the value of existing property. New residential development also often translates into more school children, whose education costs cannot always be offset by the property tax revenues generated by the new development. Additional municipal costs of development include non-education services for the community's new residents, such as new roads, sewers, and public safety. Research indicates that this local concern about municipal cost burden is justified for low and moderately priced residential development.

Examples of local restrictions that contribute to the high cost of development include: arbitrarily strict building standards, local inspectors who substitute their own building standards for the established town building codes, and restrictive zoning ordinances and bylaws such as large minimum lot sizes and low-density building requirements that require much less efficient use of land relative to existing development.

Because restrictive local policies limit development in general as well as the production of low and moderately priced houses, they have contributed to the run-up in housing prices. Reasonable easing of the controls would allow the housing supply to respond better to an increase in demand and would slow the rise in prices.

In addition to zoning and land use controls, local governments also implement other regulations that affect the cost and timing of development. Among these are the state building code and related specialty codes. Local inspectors would benefit from receiving better training to ensure that they understand and implement state codes without adding unnecessary costs. In addition, many of the codes that regulate building construction are independently promulgated by different state agencies that must coordinate to ensure there is no duplication and ensure consistency. Duplicative and inconsistent codes result in higher development costs for builders trying to comply with these codes.

[2] Turner, Margery Austin, and G. Thomas Kingsley, "*Housing Markets and Residential Mobility*" The Urban Institute Press (Washington, DC, 1993), p. 261

Another source of expense and delay in housing development is caused by the local variations in the enforcement of Title 5, the state regulation governing on-site subsurface sewage systems, including septic systems. Local septic system standards that exceed those in Title 5 have been adopted in 125 communities. Some of these local standards may be necessary because of specific local conditions, but some are not scientifically justified. In some instances, an environmental protection code intended primarily to protect water supplies can be misused to restrict land use.

Government Intervention in Housing Markets

In contrast to local government intervention in the housing market that often limits development, many federal and state policies are aimed at assisting low-income families. Each type of intervention is meant to improve the access to housing for low-income families or individuals, but they work in different ways. Demand-side policies usually involve subsidies to low-income renters; supply-side policies often offer subsidies for the construction or renovation of low-income housing; and regulatory efforts to aid low-income residents include regulations such as affordability mandates, which require builders to include less expensive units in new construction.

While the unintended negative consequences of some of these policies may hurt low-income families, some advocates of government intervention argue that the housing market is inherently unable to serve the needs of the poor. While the housing market is unlikely to produce new housing for the very poor, it can produce housing that is affordable to people with low incomes that is in many ways superior to public housing. Much low-income housing comes not from new construction but from the existing housing stock as owners trade up.

Statistical Analysis of Massachusetts Housing Production

Statistical analysis performed by the Executive Office of Administration and Finance (EOAF) suggests that the costs of new development influence communities' decisions about growth. Communities' excess levy capacity and Proposition 2½ override capacity, two variables that measure municipal budget capacity, both have a positive impact on the number of permits a community issues—towns with less ability to raise revenue issue fewer permits. This supports the idea that communities may restrict development to prevent added fiscal burden; those towns that cannot afford development do not allow it.

Special Cases

In addition to single family and multifamily housing, three segments of the housing supply requiring particular attention include student housing, single person housing, and public housing. Privately owned housing for single individuals and public housing have significant impact on the housing situation for many of those people with the lowest incomes. All three face critical difficulties that bear further discussion.

Student Housing

Students make up a large portion of the population of Boston and can have a large impact on the housing market. A policy that diverts students to dormitories will reduce the overall demand for housing and relax the pressure on the housing market. EOAF analysis confirms that the presence of large numbers of students in an area will tend to increase rents. Specifically, a 10% increase in the fraction of the community made up of students who do not live in dormitories leads to approximately a $75 increase in median rent.

The development of student housing can benefit colleges, universities, and students as well as the communities in which these institutions are located. Factors that inhibit such development include the lack of land availability, neighborhood opposition to institutional expansion, antiquated institutional guidelines for building student housing, a lack of desire on the part of some institutions to be residential real estate managers, and limits on the ability to finance new construction.

Single Person Housing

At one time, low-income single individuals had access to more low-rent options in privately owned housing, but over the past several decades, the number of these options has declined. Between 1965 and 1985, Massachusetts experienced a 96% drop in single room occupancy units, the largest drop in the country. Many of the Commonwealth's homeless shelter providers have suggested that a lack of low-cost rental housing for single adults has contributed to the growing number of homeless individuals.

It is important to note that many homeless and at-risk single persons facing a temporary crisis may only be in need of low-cost housing that is safe and secure, such as a room for rent in a safe and well run facility. Other at-risk single persons with specific physical and mental health issues may need a room or apartment of their own with supportive services available.

Public Housing

In this time of rising rents and demands on the homeless shelter system, the Commonwealth's 50,000 units of state-aided public housing are an increasingly important resource. In the early days of the state's public housing program when the housing stock was relatively new, the need for capital improvements was limited. Today, the average age is 34 years and climbing. The size of this aging portfolio makes it difficult to keep pace with capital needs. In addition to capital improvement needs, the public housing portfolio also finds itself hamstrung by a statutory framework that limits the flexibility of local housing authorities to respond to local needs or changes in the local housing market.

Affordable Housing in Massachusetts

The federal government over much of the twentieth century created and expanded a series of programs intended to provide housing for low-income households, including public housing, privately owned assisted housing, Section 8, and tax credits and tax-exempt bonds.

Almost uniquely among states, the Commonwealth has significantly augmented the housing produced by a series of federal programs with substantial assisted housing programs of its own. These include public housing, rental assistance and project-based subsidy of privately owned assisted housing, state aid for rental production, financing through the Massachusetts Housing Finance Agency and the Massachusetts Housing Partnership Fund, and other ongoing state capital funding for affordable housing. New funding initiatives include the State Low Income Housing tax Credit Program and the State Affordable Housing Trust, which together will make $200 million available to be committed over the next five years for the development and rehabilitation of affordable housing and the promotion of home ownership. The Cellucci-Swift Administration is also advocating for long-overdue increases in the federally-imposed per capita limits on low-income housing tax credits and on tax-exempt private activity bonds that can be used to finance affordable housing development and preservation.

The result of a half-century of affordable housing programs is that a significant portion of the Massachusetts rental housing market is subsidized in one way or another. Nearly one-quarter of Massachusetts rental tenancies either exist in units developed, rehabilitated, or operated using public subsidies or are occupied by tenants who have rental subsidies. Such a high number of Massachusetts tenancies are subsidized because of both a disproportionate share of federal housing assistance and the addition of tenancies subsidized by sizable state programs. Together, state and federal programs spend more than $1.3 billion per year to build, renovate, or subsidize the operation of affordable housing and for rental subsidies in Massachusetts. Departments in the state Executive Office of Health and Human Services spend an additional $1.1 billion annually to provide housing and related services to their clients.

Action Agenda

While these affordable housing programs have created a large number of housing units and subsidies that allow low- and moderate-income people to pay varying levels of below-market rents, they have not been able to arrest the increase in housing costs for renters and prospective homeowners across the income spectrum. The scarcity of supply means that middle and upper income households have needed to look to communities, neighborhoods, and buildings that had traditionally housed families and individuals of more modest means. This has the result of displacing low-income households from such communities.

There are two ways to address this situation. One is for the government to provide an affordable unit or a subsidy for the low-income family. The other is to free the private market to produce enough units for the market-rate household. Massachusetts does a great deal of the former, has done so tracing back to 1948, and has plans to continue using existing and new programs. But that alone has not proved to be enough, especially in the current environment of high housing demand. Improvement of the operation of the private housing market can bring capital to bear for the expansion of the housing supply to a degree that government cannot match. Because the private real estate development industry is so much larger than public sector programs, a 10% increase in overall housing production would have an effect on the Massachusetts housing supply equivalent to doubling government financing of new affordable housing development.

The following lays out an agenda of some initiatives already underway and others that need to be launched to eliminate needless barriers to development in order to address the need for more housing in Massachusetts. These initiatives seek to help communities move forward through incentives, rewards, and a new approach in which local aid is allocated to offset the incremental municipal costs resulting from new housing development priced at the middle and lower end of the market.

Executive Order 418

To help communities reduce local barriers and address the housing shortage, Governor Cellucci issued Executive Order 418 (E.O. 418) on January 21, 2000. E.O. 418 helps communities plan for future development by providing up to $30,000 in grants and technical assistance and gives priority in awarding $364 million in state discretionary funds to those cities and towns that take steps to increase the supply of housing.

Special Commission on Barriers to Housing Development

To engage a broader spectrum of interested parties in the formulation of strategies to address the state's housing problem, the Cellucci-Swift Administration will establish a special commission on barriers to housing development. The commission and its working groups will systematically review government-imposed barriers to residential development and recommend to the Governor specific legislative, regulatory, policy, and operational changes beyond those discussed in this report that are needed to remove unnecessary state and local barriers. In relation to the initiatives discussed in this report, the commission will examine and make recommendations regarding zoning and land use controls, local enforcement of building and related specialty codes and the implementation of expanded training for local officials, and local septic system standards exceeding those prescribed by Title 5. The commission will submit their recommendations to the Governor and Lieutenant Governor by June 30, 2001.

Housing Supply Incentive Program

To address the costs new development imposes on local budgets, particularly the education costs, that cause many communities to resist the construction of low- and moderately-priced housing, Governor Cellucci included in his fiscal year 2001 budget proposal the Housing Supply Incentive Program, funded at $47 million per year. This program would pay the difference between what a community could expect to receive in tax revenue from new development and the costs of educating the school children anticipated to result from such development. Based on research by the Executive Office of Administration and Finance, the Governor's fiscal year 2001 budget proposal offered aid to make up for net costs for housing units valued up to $220,000 and offered extra aid for multifamily development.

The Housing Supply Incentive Program was not included by the legislature in the state's fiscal year 2001 budget. It still needs legislative approval, and it will be pursued once again in the next legislative session.

Expanding the Economic Development Incentive Program

In order to provide financial aid and incentives for housing development, including affordable housing, Governor Cellucci and Lieutenant Governor Swift on June 22, 2000 filed H. 5285, entitled "An Act Creating a Pilot Expansion of the Economic Development Incentive Program to Include Affordable Housing Development Projects." The proposed act would extend the benefits currently available under the Economic Development Incentive Program to the development of affordable housing.

The legislature's Joint Committee on Housing and Urban Development committed the bill to study, and it was not taken up by the House of Representatives or the Senate during the 2000 legislative session.

Streamlining the Disposition Process for Surplus State Property

By identifying and making available surplus state property that is suitable for development, the Commonwealth can contribute to improvement of the housing problem. On June 22, 2000, Governor Cellucci and Lieutenant Governor Swift filed H. 5286, entitled "An Act Facilitating the Development of Underused Facilities and Properties for Housing in the Commonwealth." The Cellucci-Swift Administration's bill streamlines the disposition process for unneeded parcels of state land that can be used for housing development. The streamlined process could save a year or more compared to the current process. Property disposed of under this act would be subject to reuse plans approved by affected communities.

The bill was referred to study by the legislature's Joint Committee on Housing and Urban Development and was not taken up by the House of Representatives or the Senate during the 2000 legislative session.

Improving the Climate for Rental Housing

Current operation of tenant-landlord law in Massachusetts discourages some owners of rental properties from renting their apartments and contributes to abandonment of rental properties, thereby contributing to the state's rental housing supply problem. For example, tenants can abuse the right to withhold rent under current Massachusetts law by doing so even if their apartments do not have substantial code violations. By the time the matter is adjudicated, several months' rent may have been withheld, and even if a landlord prevails and a court orders that the tenant pay back rent, funds are often not available to satisfy the judgment of the court. It is necessary to make the lawful withholding of rent more about the condition of an apartment and less about missed payments

The Administration will submit legislation in the 2001 session that aims to protect stability in rental housing by enacting a requirement that tenants place rent in escrow if they withhold it claiming substandard conditions. The bill will protect landlords against tenants who abuse the habitability defense while providing adequate consumer protections for tenants with bad landlords. The Administration's bill will strike this balance and help ensure that landlords do not hold their rental properties offline for fear that abuse of the laws will leave them with an unreliable source of rental income.

Improving the Regulatory Environment for Residential Development

To improve the regulatory environment for development and construction, it is necessary to reexamine the implementation of state regulations and policies that affect housing construction and development. State agencies must work with their local counterparts to ensure that the protections intended by these codes are effectuated without unintended development restrictions.

Building Codes and Related Specialty Codes

Because there are numerous boards and state agencies independently promulgating the codes that regulate building construction, the Commonwealth will sometimes put into place regulations that are conflicting or duplicative. To address these issues, Governor Cellucci and Lieutenant Governor Swift will issue an executive order to identify, resolve, and prevent conflicting and duplicative regulations related to building construction and rehabilitation. In addition, an expansion of state-funded training for local building and fire prevention officials and local plumbing, gas, electrical, and health inspectors will lead to more uniform and predictable enforcement of codes.

The working group will also recommend mechanisms to ensure that local officials involved in inspection of approval of construction have appropriate oversight and accountability so that inspections and approvals are consistently timely and appropriate. Areas to be examined include licensure processes to deal with complaints and administrative appeals mechanisms for local inspectors' and safety officials' decisions.

Finally, the working group will review the formal local imposition of building requirements without legal authorization. The group will determine the prevalence of such requirements and, if warranted, recommend corrective action.

Title 5

Discussions with representatives of the residential development industry indicate that another source of expense and delay in housing development is the local enforcement of Title 5 (310 CMR 15), the state regulation governing on-site subsurface sewage systems, including septic systems. Standards stricter than those in Title 5 should not normally be necessary, yet 125 communities have adopted such standards. The Governor's special commission on local barriers to housing development will be charged with examining the adoption of standards in excess of Title 5 and the enforcement of Title 5 and local septic system bylaws. With the assistance of the state Department of Environmental Protection (DEP), the commission will determine the frequency with which local standards are stricter than what is required by scientifically valid environmental protection needs. The commission will recommend measures that would ensure that localities impose standards that are no stricter than necessary for natural resource protection.

In addition, DEP will evaluate its training and outreach efforts to determine if they should be expanded or intensified. As part of this process, DEP will develop a plan for targeted outreach and training for communities that may have adopted needlessly restrictive local requirements.

Single Person Housing

In order to expand the array of options available that are appropriate for and affordable to low-income, single person households, the Commonwealth must facilitate the development and rehabilitation of such housing. Three initiatives that aim to accomplish this goal involve:

- reserving funding and project-based vouchers for the development of single-person housing;
- instituting an education program on single person housing for developers, communities, and other interested parties; and
- identifying and addressing barriers to the effective use of the Facilities Consolidation Fund for the development of single person housing.

State-Aided Public Housing

To preserve the continued viability of public housing as the portfolio ages, on-going capital needs of the public housing stock must be addressed. Attending to these needs will extend the life of the structures and improve the quality of life of its residents. The cost-effective revitalization of public housing can be accomplished by focusing on several key steps.

1. Planning and funding capital improvements

    - Move toward better local, development-based, long-range capital planning that is essential to the proper asset management of a real estate portfolio.
    - Use leveraged financing to attract private financing for public housing modernization. Tapping this funding source could provide millions in additional funding each year.

2. Statutory changes generating financial efficiencies for public housing and local housing authorities

Promoting the Development of Student Housing

Increasing student housing decreases pressure on local rental markets while at the same time making universities more attractive to potential applicants. Done correctly, it can also provide a rationale and serve as a process to bring communities and institutions together around a common goal, helping to build the bonds of trust between colleges and universities and their host neighborhoods. The following initiatives aim to accomplish this goal:

- Build on the Davenport Commons model implemented by Northeastern University, the City of Boston, and the Commonwealth. The model combines state assistance for building affordable housing for the community with the school's construction of student housing to help ease neighborhood resistance and make financing work.

- Work with existing university consortia and umbrella organizations to build joint housing facilities.

- Encourage universities to review building guidelines to lower costs and take advantage of the newest technologies.

- Create a partnership between universities and MHFA to assist first-time homebuyers of two to three family buildings to provide scattered site student/faculty housing and stabilize neighborhoods.

- Encourage universities to build partnerships with their communities.

Conclusion

Over the last year, the Cellucci-Swift Administration has been examining the causes and effects of the excessively tight housing market in Massachusetts. It is clear that housing affordability is becoming a greater problem as the housing market fails to respond to price increases with the increased production that one would expect. Traditional affordable housing programs help those who have a housing subsidy, but they have not and cannot address the wider problem of affordability caused by production impediments that do not allow market forces to work as they should.

The state continues its commitment to affordable housing through an expansive array of programs. We must, however, look beyond government programs to long-term solutions. The program outlined in this report shows a way toward real, long-term answers. But the state's housing development problems are not easily solved. They are complex and have been years in the making. Their solution will require an ongoing commitment on the part of those who appreciate the issue's importance to make improvements in the processes that surround housing production. Equally important, however, the public must more widely be made to understand how critically important it is to remove barriers to housing development so that the housing needs of the Commonwealth's residents can better be served. Bringing down the barriers to change the housing supply dynamics in Massachusetts is essential. The quality of life in our state and our economic future depend on it.

Introduction

Over the last few years, Massachusetts has enjoyed remarkable economic prosperity, a situation far different than it was ten years ago. Then, Massachusetts was in the midst of a severe recession, as real median household income fell more than 10 percent, and unemployment rose to nearly that rate. Today, incomes are rising; at the end of 1999, per capita personal income in the Commonwealth was tied for second among the states. Massachusetts now also enjoys the lowest unemployment rate among the major, industrialized states. In the last 30 years, the state has had an unemployment rate below three percent in only eight months; six of them have been in 2000. While Massachusetts' economic fortunes fell further than the nation's during the recession of a decade ago, its recovery has outpaced the nation's.

Our newfound prosperity, however, has brought with it a troubling consequence – rising housing costs and a corresponding shortage of homes for our citizens. The prices of houses and rents have increased at a rate faster than incomes in much of the Commonwealth. While these increases have benefited those who were already homeowners, they have had negative effects for renters, for those who wish to become homeowners, and for anyone considering moving to Massachusetts from another area of the country. Excessively high housing price increases have led to troubling distributional effects among existing residents of the state. They also threaten the state's continued economic vitality by reducing the state's competitiveness and making it harder to attract new residents, contributing to a labor shortage in many sectors of the economy.

One might expect that increased housing prices would lead to increased production, but that has not been the case. Building permits for new residential construction have remained at their 1992 levels, leaving Massachusetts 47th in the nation for building permits per capita. Permits for housing units in multifamily buildings are at slightly more than one-third the per capita national rate. The amount of housing supplied in Massachusetts has not kept pace with demand. Housing production has trailed national rates, even as price increases have led the nation.

What is different about Massachusetts that causes the rising prices and stagnant supply we have experienced, and what can be done to address the problem?

Some have suggested that the solution to the state's housing supply problem lies in expanding government subsidy programs. Such an approach is hardly novel. Since the Great Depression, the federal government has funded the development of subsidized-housing and, more recently, provided rental assistance to households. To substantially augment these federal programs, Massachusetts has been a national leader in the production of state-subsidized housing for more than a half century. Together, state and federal programs subsidize approximately one-quarter of all rental tenancies in the Commonwealth. Yet Massachusetts's rate of growth in house prices since 1980 is by far the greatest in the country, and rents have outstripped the ability to pay of many low- and moderate-income households who do not benefit from subsidies.

What makes Massachusetts different is not that we subsidize less housing than other states—we actually subsidize more. Rather, the key difference is that the private sector here produces less housing to meet demand than it does in other parts of the country. Systemic problems have prevented the private market from responding to increased demand by building enough new homes.

Some of these problems are unavoidable: Massachusetts is an old, relatively densely settled state, and that inherently limits land available for development. But many of the problems are of our own making. Regulations and processes—from zoning to building codes to Title 5—can unnecessarily add cost and delay housing development. They can be and too often are used locally as the instruments of a policy of "not in my back yard," rather than for the legitimate planning, safety, and resource protection purposes for which they were created. And when communities impede new housing projects in pursuit of particular local interests, it ultimately imposes broader social and economic costs.

This report examines housing price (including rents) and production trends in Massachusetts. It discusses local barriers to housing development. It provides some empirical evidence that the degree of restriction on housing does depend, in part, on local financial capacity—communities with the least capacity to collect additional property tax revenues tend to have less development. It discusses the impact that students have on the Boston rental market, indicating that each additional 10% of a neighborhood's residents who are students living in private apartments leads to a $75 increase in median rent. It discusses two housing resources critical to low-income people, especially in the current tight housing markets: single-person housing and public housing. Finally, it lays out a program of initiatives to remove unnecessary barriers to housing growth.

The Cellucci-Swift Administration has already undertaken some of these initiatives, but others require legislative action. A special commission on barriers to housing development will continue to examine the problem and make recommendations for further action, especially in areas identified in this report. The commission will also serve to increase the involvement of public officials and private citizens in this critical issue—one which will require not only regulatory and program reforms, but also changes in understanding and attitudes among government bodies and the citizenry.

Recently, the Archdiocese of Boston released a study titled "A New Paradigm for Housing in Greater Boston." In this new paradigm, actors at all levels of government and across society must recognize the need for additional housing supply and overcome the social, economic, and political barriers to its development. Such a transformation in opinion and action will be necessary for progress to be made on the housing issue. The course forward described in this report depends on it.

This report culminates months of effort by the Cellucci-Swift Administration to improve the housing climate in Massachusetts. It is, however, the end only of the first phase of a continuing process. The Administration remains committed to finding solutions to our housing needs and will continue to push forward to spur housing development that meets the needs of Massachusetts residents.

The Parameters of the Current Problem

Housing Prices

The most widely felt consequence of the current housing shortage is the rapid growth of housing prices and rent in Massachusetts. The rising prices increase the housing cost and rent burden faced by all but the most affluent of the Commonwealth's households, make it difficult for people to live in the communities in which they grew up or currently work, and hurt the economic competitiveness of the state to the extent that businesses and employees choose to locate in states with lower housing costs.

Measurements indicate that both house prices and rents are on the rise. According to Office of Federal Housing Enterprise Oversight (OFHEO), housing prices in Massachusetts are rising faster than in any other state. As of the end of the second quarter of 2000, OFHEO's House Price Index[3] for Massachusetts was growing at an annual rate of 13.7%, about twice the national average. Since 1980, house prices in the Commonwealth have increased by 326%, as compared to the national average of 143%. New York was the only other state in the country where prices increased by more than 190%. House prices in Massachusetts are up by 32.7% compared to their 1989 peak of the 1980s cycle, up by 49.4% over their low point in 1992 after that peak, and up by 35.9% since the beginning of 1997. At the local level, Massachusetts accounted for three of the twenty Metropolitan Statistical Areas (MSAs) with the fastest growing housing prices in the U.S. during the year ending in June 2000, and another Massachusetts MSA ranked 21st in the nation.[4]

Because the House Price Index (HPI) draws upon repeat sales data from Fannie Mae and Freddie Mac, only existing low to moderate priced houses are included in the sample. The data, therefore, do not take into account the systematic differences between existing homes that are put on the market and those that are newly constructed. While in the past developers built modest starter homes, recent building has predominantly consisted of higher priced trade-up and second homes.[5] The HPI also excludes jumbo mortgages, which, according to the Massachusetts Association of Realtors (MAR),[6] is where the increases in current sales are occurring.[7]

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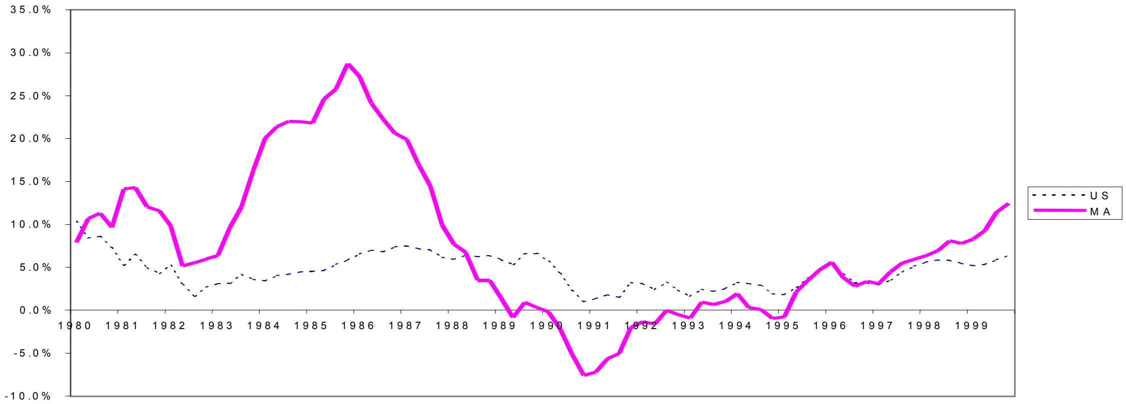
[3] OFHEO's House Price Index (HPI), a modified version of the Case-Shiller repeat sales price index, measures the annual rate of price change for sales of the same houses, thereby isolating market effects from price changes caused by differences in the mix of houses sold. The HPI is a weighted repeat sales index based on over 12.5 million transactions involving conforming, conventional mortgages purchased or securitized by Fannie Mae and Freddie Mac over the past 20 years. As of January 2000, the conforming limit for single-family houses was $252,700. Properties whose mortgages are insured by the federal government (e.g. FHA, VA), or are not sold into the secondary market (including expensive properties whose mortgages exceed the conforming loan limit), and properties acquired without a mortgage are not included in the index.

[4] Out of 180 ranked MSAs nationwide, Barnstable-Yarmouth ranked 7th with an annual growth rate of housing prices of 17.1%, Boston ranked 11th with a growth rate of 15.2%, and Lowell ranked 13th with a growth rate of 14.9%. Lawrence was 21st in the nation with a growth rate of 12.6%.

[5] Comment by Nick Retsinas, Director of the Harvard Joint Center for Housing Studies, at the CHAPA seminar on "State of the Nation's Housing" on August 1, 2000.

[6] Sales and price data from the MAR reflect transactions occurring through Realtor-affiliated multiple listing services in the Commonwealth and account for approximately 50 percent of all real estate sales in Massachusetts.

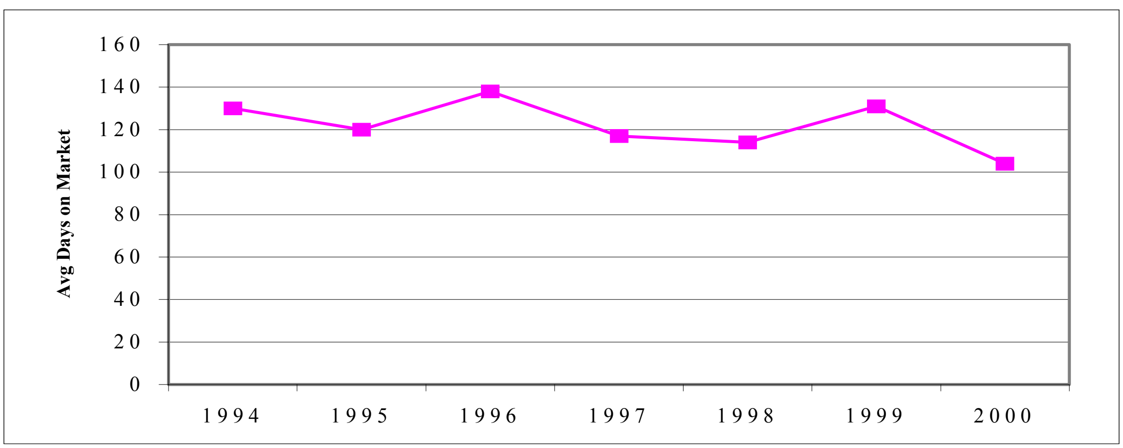
Figure 1: Annual Percent Change in Repeat-Sales House Price Index, 1980-1999



Source: Office of Federal Housing Enterprise Oversight

According to MAR, the limited inventory of houses for sale contributes to the upward pressure on housing prices. The scarcity of available homes is illustrated by the decline in the average number of days units spend on the market. As seen in Figure 2, detached single-family houses are remaining on the market for fewer days on average in 2000 than they had in the previous six years.

Figure 2: Average Number of Days Single-Family Houses Spend on the Market, 1994-2000



Source: John Dulczewski, Massachusetts Association of Realtors

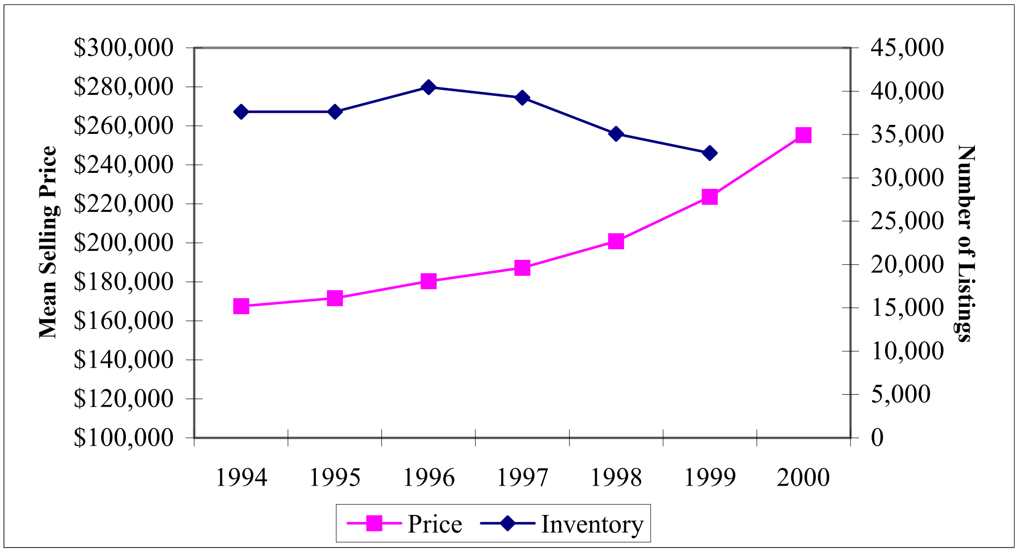
Between the second quarter of 1999 and the second quarter of 2000, the number of single-family listings declined by 16.9% statewide.[8] During that same time period, the statewide average

[7] "*Bay State Housing Market Cools in Spring Quarter, But High-end Home Sales Heat Up*" Massachusetts Association of Realtors Press Release (August 9, 2000)

[8] One potential explanation for the decline in houses listed with brokers is that the strong housing market is making it more feasible for owners to sell their homes without the assistance of a real estate agent. Alternatively, because homes sell quickly, each home spends less time on the market, so that at any time there are fewer total listings.

selling price for detached single-family houses rose by 20.1 percent from $239,399 to $287,493.[9] Annualized data from MAR clearly show the accelerating upward trend in prices and the simultaneous decline in inventory.

Figure 3: Single-Family Listings and Average Selling Price, 1994 – 2000



Source: John Dulczewski, Massachusetts Association of Realtors

MAR President Fred Meyer conjectures that "the primary cause for the spike in average prices, however is the boom in upscale, primary and second home sales, which have risen sharply this past year…. The sale of just a few higher-priced homes has driven up the average selling price sharply."[10] However, median house prices are also on the rise. Housing advocates argue that dramatically increasing prices have been "catastrophic for renters and potential first-time home buyers."[11]

Rents

Rental prices in major Massachusetts markets are also on the rise. Table 1 compares the American Housing Survey Metropolitan Sample data for Boston in 1993 and 1998 to see if there are systematic differences in rent level.[12] As can be seen below, median rent rose in all multifamily categories between 1993 and 1998. The 61.3% increase in rent for units in structures with 50 or more units in them is likely to reflect the development of some new large

9 Massachusetts Association of Realtors Press Release (August 9, 2000). This is an average sale price, rather than a median sale price such as is tracked by the Repeat Home Sale Index. Average house prices will usually exceed medians, because very highly priced houses have a disproportionate effect.

10 Massachusetts Association of Realtors Press Release (August 9, 2000).

11 Grillo, Thomas, "*Home Prices Climbing Despite Slowing Sales*" Boston Globe (August 19, 2000), p. E01.

12 This is a longitudinal study that surveys the same units in both years when possible. Exceptions to this are new units that are added to reflect new construction and others that are removed from the survey when they no longer exist.

luxury apartment buildings and may also reflect a greater tendency of professionally managed properties to capture the highest rent the market will bear.

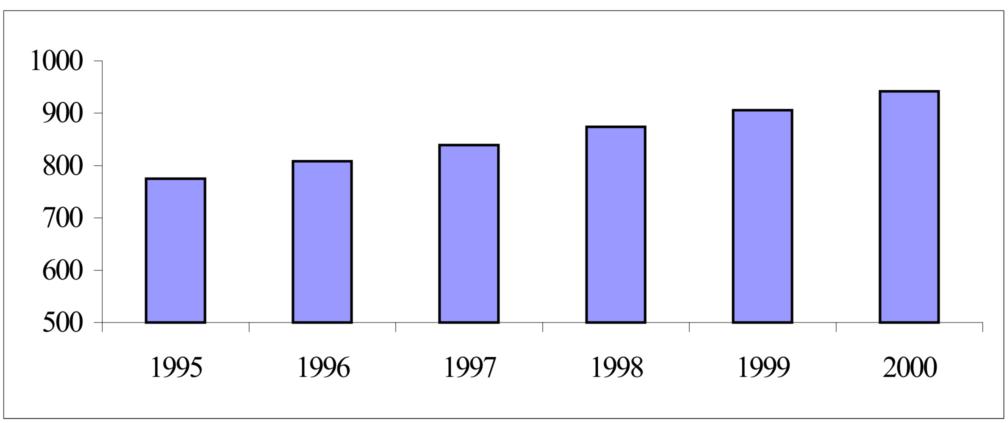
Table 1: Median Rent in Boston Metropolitan Area by Number of Units per Structure, 1993 and 1998

Units Per Structure	Median Rent 1993	Median Rent 1998	% Change
2-4	568	764	34.5%
5-9	575	665	15.7%
10-19	609	711	16.7%
20-49	644	727	12.9%
50 or more	380	613	61.3%

Source: U.S. Department of Housing and Urban Development, Boston Metropolitan Area Survey

The Rental Housing Association's 1997 survey of rents indicates a 13.73% increase in rent from $920 to $1,047 in the Greater Boston Area between fall 1996 and fall 1997.[13] More recent analysis performed by the Boston Department of Neighborhood Development indicates that Boston's median advertised asking rent increased by 9% to $1,465 in the year ending in the first quarter of 2000, up from $1,350 in 1999. Some of Boston's lower rent neighborhoods such as Dorchester, Roslindale and Roxbury witnessed among the highest increases in advertised rents, ranging from 13 to 15 percent.[14] The U.S. Department of Housing and Urban Development's (HUD) Section 8 Fair Market Rents (FMRs) in the Boston Metropolitan Statistical Area rose from $775 in 1995 to $942 in 2000, an increase of 22%.[15]

Figure 4: Average Monthly Two Bedroom Fair Market Rents in Boston, 1995-2000



Source: U.S. Department of Housing and Urban Development

[13] "*The Rental Housing Association Industry Survey: Tri-Annual Report*" (Fall 1997). Note: The survey only covers properties of RHA members, which tend to include larger buildings.

[14] Housing Foreclosures and Rents, First Quarter Report 2000, Department of Neighborhood Development, Research and Development Unit.

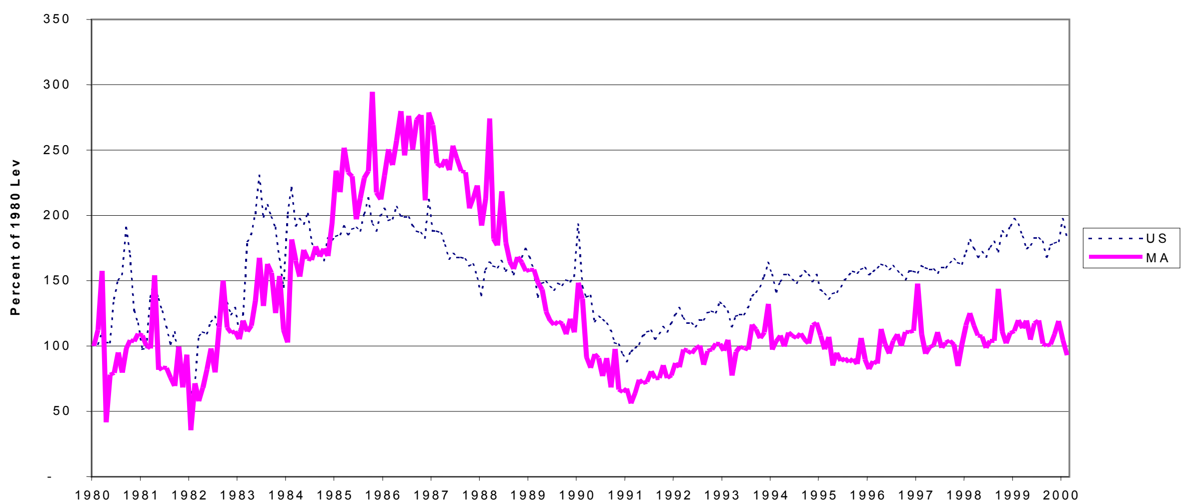
[15] Fair Market Rents are HUD's estimate of the 40th percentile rent for new tenancies.

Construction Activity

The increase in housing prices can be explained by changes in supply and demand. Despite the price increases, there has not been an increase in the growth rate of Massachusetts' housing stock – the supply of housing has remained relatively unchanged. The number of building permits issued annually for new residential construction is not only well below the annual production levels the state experienced in the real estate boom of the mid-1980s, but it is up only slightly since the trough of the recession of the late 1980s and early 1990s.

The growth in the number of permits issued in Massachusetts paralleled or exceeded the national trend through the 1980s.[16] Since 1992 however, the number of permits in the Commonwealth has remained relatively constant between 18,000 and 19,000 per year while the average number of permits issued nationwide has risen. Net new growth in single-family parcels between 1992 and 1998 is flat at about 12,500 per year. The fact that housing construction, as measured by the number of permits issued, has remained constant despite price increases indicates that there are constraints that make the supply of housing in Massachusetts relatively inelastic. The shortage of land available for residential development combined with restrictions associated with building make it more difficult for suppliers in Massachusetts to respond to changes in demand for housing.

Figure 5: Total Housing Permits Authorized Relative to 1980, 1980-2000



Source: U.S. Census Bureau Construction Statistics, <www.census.gov/ftp/pub/const/www/c40index.html>

As seen in Table 2 below, production in Massachusetts clearly lags behind comparable states. In 1999, Massachusetts ranked 47th in the nation in terms of the number of permits per capita issued the lowest number of permits per capita of any state the Northeastern and industrial states with the exception of New York. Massachusetts had only 40% of the national rate of permits per capita and only 35% of the national rate for multifamily permits.

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[16] Permits authorized are a measure of construction activity, but this measure does not provide an exact count of new units actually constructed, because projects for which permits are pulled are sometimes not built. Permit data does, however, reflect the trend in construction activity over time.

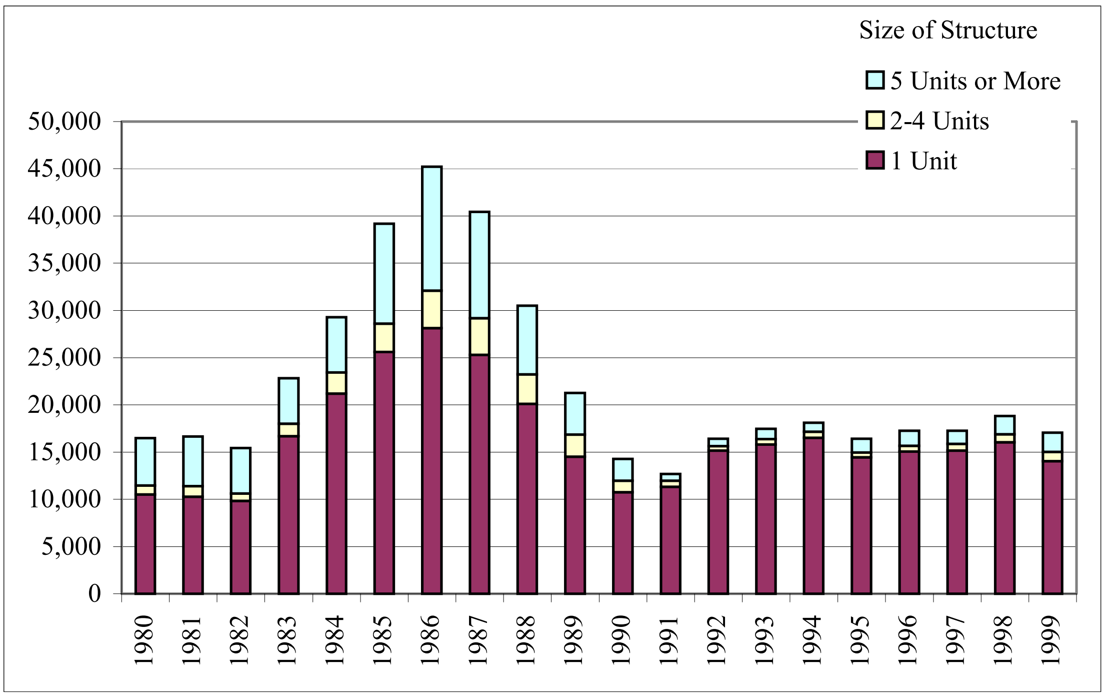
Table 2: Permits and Population by State, 1999

	Total Permits (1999)	Single Family Permits	Multi-family Permits	Population	Total Permits Per 1,000	Single Family Units Per 1,000	Multi- Family Units Per 1,000
Nevada	32,663	24,271	8,392	1,676,809	19.48	14.47	5.00
Arizona	63,951	52,118	11,833	4,554,966	14.04	11.44	2.60
Colorado	48,874	38,267	10,607	3,892,644	12.56	9.83	2.72
Georgia	91,044	71,817	19,227	7,486,242	12.16	9.59	2.57
North Carolina	84,309	63,754	20,555	7,425,183	11.35	8.59	2.77
Florida	163,148	105,107	58,041	14,653,945	11.13	7.17	3.96
Idaho	11,550	9,918	1,632	1,210,232	9.54	8.20	1.35
South Carolina	35,717	26,557	9,160	3,760,181	9.50	7.06	2.44
Utah	17,743	14,281	3,462	2,059,148	8.62	6.94	1.68
Virginia	52,997	42,254	10,743	6,733,996	7.87	6.27	1.60
Washington	43,850	29,598	14,252	5,610,362	7.82	5.28	2.54
Texas	144,914	100,143	44,771	19,439,337	7.45	5.15	2.30
Delaware	5,288	4,825	463	731,581	7.23	6.60	0.63
Minnesota	33,510	26,176	7,334	4,685,549	7.15	5.59	1.57
Tennessee	38,113	31,462	6,651	5,368,198	7.10	5.86	1.24
Indiana	40,881	33,517	7,364	5,864,108	6.97	5.72	1.26
Oregon	22,605	16,217	6,388	3,243,487	6.97	5.00	1.97
Wisconsin	33,470	23,325	10,145	5,169,677	6.47	4.51	1.96
Maryland	29,472	24,028	5,444	5,094,289	5.79	4.72	1.07
Kansas	14,697	10,732	3,965	2,594,840	5.66	4.14	1.53
Kentucky	21,642	16,604	5,038	3,908,124	5.54	4.25	1.29
New Mexico	9,559	8,640	919	1,729,751	5.53	4.99	0.53
Nebraska	8,918	6,547	2,371	1,656,870	5.38	3.95	1.43
Michigan	52,560	43,555	9,005	9,773,892	5.38	4.46	0.92
South Dakota	3,964	3,002	962	737,973	5.37	4.07	1.30
New Hampshire	6,051	5,568	483	1,172,709	5.16	4.75	0.41
Ohio	55,774	40,041	15,733	11,186,331	4.99	3.58	1.41
Missouri	25,373	19,844	5,529	5,402,058	4.70	3.67	1.02
Arkansas	11,682	7,973	3,709	2,522,819	4.63	3.16	1.47
Mississippi	12,282	9,409	2,873	2,730,501	4.50	3.45	1.05
Vermont	2,641	2,218	423	588,978	4.48	3.77	0.72
Iowa	12,758	9,897	2,861	2,852,423	4.47	3.47	1.00
Alabama	19,311	16,172	3,139	4,319,154	4.47	3.74	0.73
Maine	5,506	5,151	355	1,242,051	4.43	4.15	0.29
Illinois	52,515	39,456	13,059	11,895,849	4.41	3.32	1.10
California	135,032	100,157	34,875	32,268,301	4.18	3.10	1.08
Oklahoma	13,293	10,728	2,565	3,317,091	4.01	3.23	0.77
New Jersey	32,159	25,344	6,815	8,052,849	3.99	3.15	0.85
North Dakota	2,556	1,472	1,084	640,883	3.99	2.30	1.69
Louisiana	17,210	13,486	3,724	4,351,769	3.95	3.10	0.86
Wyoming	1,798	1,444	354	479,743	3.75	3.01	0.74
Alaska	2,205	1,537	668	609,311	3.62	2.52	1.10
Pennsylvania	40,903	34,785	6,118	12,019,661	3.40	2.89	0.51
Rhode Island	3,304	2,639	665	987,429	3.35	2.67	0.67
Hawaii	3,955	3,143	812	1,186,602	3.33	2.65	0.68
Connecticut	10,898	9,566	1,332	3,269,858	3.33	2.93	0.41
Massachusetts	**18,545**	**15,249**	**3,296**	**6,117,520**	**3.03**	**2.49**	**0.54**
Montana	2,390	1,472	918	878,810	2.72	1.67	1.04
West Virginia	4,440	3,389	1,051	1,815,787	2.45	1.87	0.58
New York	41,517	24,637	16,880	18,137,226	2.29	1.36	0.93
Dist. of Colum	683	319	364	528,964	1.29	0.60	0.69
Totals	**1,640,220**	**1,231,811**	**408,409**	**267,636,061**	**6.13**	**4.60**	**1.53**
Massachusetts As a Percent of Average					*49%*	*54%*	*35%*

Source: U.S. Census Bureau Construction Statistics, <www.census.gov/const/www/index.html>

While growth rates for all types of housing have declined since the boom of the late 1980s, the change in multifamily housing starts is particularly striking. Multifamily developments play an important role in creating lower cost housing. They also increase the stock of rental housing and can be sited near public transportation, which leads to reduced reliance on automobiles and consequently less traffic and fewer emissions. A decrease in multifamily development exacerbates the affordability problem, particularly since renters typically have lower incomes than do owners. In addition, multifamily development is more dense than single-family development and is therefore less likely to lead to urban sprawl. Multifamily permits in the Commonwealth, though up slightly in the last two years, are at less than half their 1989 level. In the 1980s, multifamily permits averaged 6,792 per year; in the 1990s they averaged only 1,317.

Figure 6: Number of Permits for New Housing Construction by Size of Structure, 1980-1999

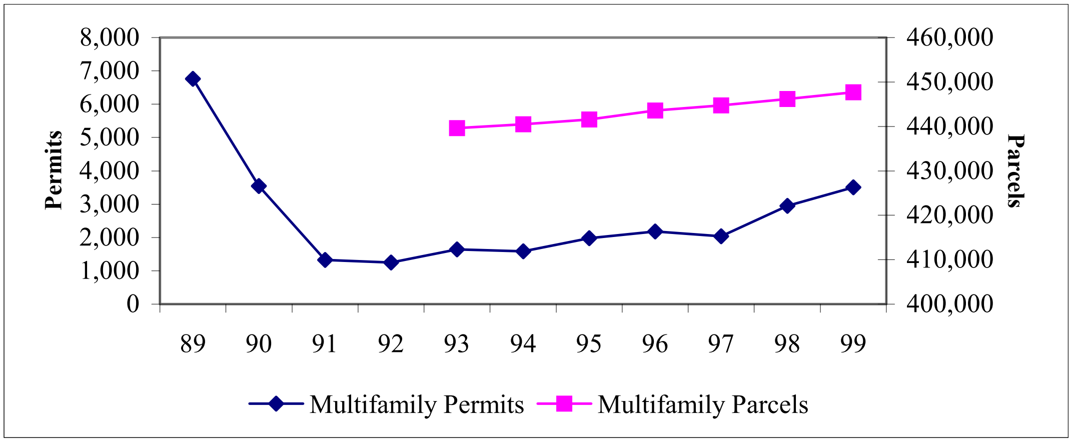


Source: U.S. Census Bureau Construction Statistics, <www.census.gov/const/www/C40/table2.html>

The number of multifamily permits[17] dropped sharply between 1989 and 1991. Between 1991 and 1997, the number of multifamily permits rose slightly. Since 1997, there has been a small increase in multifamily permits issued, but the number of permits is still far from its peak in the late 1980s and is even below the number issued in the years before the 1980s real estate boom. These multifamily permits translate into moderate growth in the stock of multifamily parcels since 1993. However, the construction of new condominium buildings accounts for this growth; the number of parcels containing multifamily rental units has remained constant.

[17] For the purpose of this discussion, a multifamily unit is defined as being any unit in a building containing two or more units.

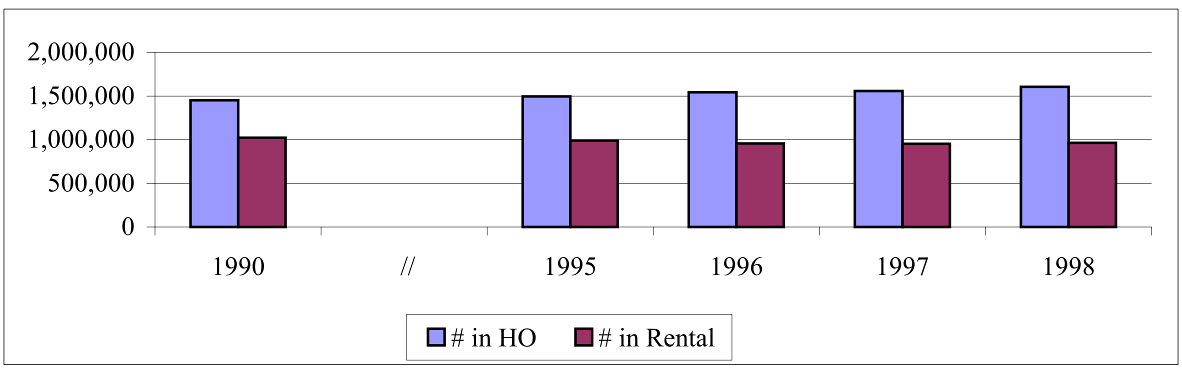
Figure 7: Multifamily Permits and Parcels, 1989-1999



Source: U.S. Census Bureau; Massachusetts Department of Revenue, Division of Local Services

The combined impact of the decline in multifamily starts and conversion of multifamily buildings into condominiums on rental and ownership units can be seen in Figure 8.

Figure 8: Massachusetts Homeownership Households versus Rental Households, 1990-1998



Source: U.S. Census Bureau, Housing Vacancies and Homeownership, <www.census.gov/hhes/www/hvs.html>

The construction of multifamily units that is occurring is concentrated in relatively few cities and towns. The top 10% of communities ranked by number of multifamily permits issued account for 83% of multifamily permits in the Commonwealth but only 32% of the state's population. The top 5% of communities account for 68% of multifamily permits and 21% of the population, while the top 10 communities account for 57% of the multifamily permits issued and only 16% of the population.[18]

Had multifamily construction occurred at the same rate in the 1990s as it did in the 1980s, more than 50,000 additional units would have been built. It should be acknowledged that multifamily properties were developed at aberrantly high levels in the 1980s, but even if 1990s development had occurred at one-half the 1980s rate, it would have created an additional 25,000 units. That is more than two and one-half times the number of units produced by the largest state housing production program of the 1980s. Had new residential building permits been issued in

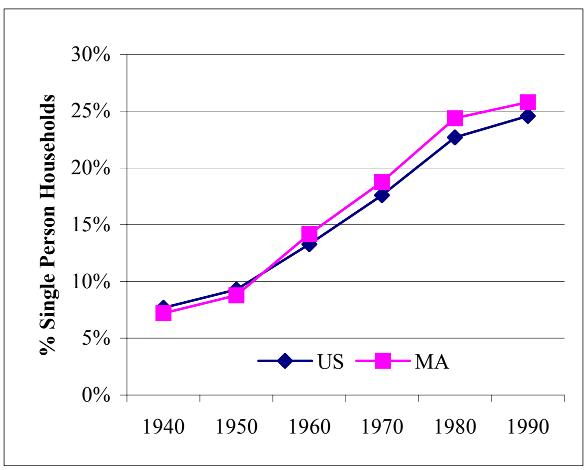
[18] Permit data for 1997-99 from U.S. Census Bureau, www.census.gov/ftp/pub/const/www/c40index.html , 1998 population estimate (U.S. Census Bureau).

Massachusetts in 1999 at the same per capita rate as the United States average, the result would have been an additional 18,703 permits in the Commonwealth, 5,931 of which would have been for multifamily units. That would have represented a 99% increase over the actual number of total permits issued and a 169% increase in the number of permits for multifamily units issued. That does not necessarily suggest that residential development in Massachusetts *should* occur at the same rate as it does in the nation as a whole, but it does indicate that the state's housing supply and demand imbalance could be reduced if the rate of new construction at least more closely resembled the nation's.

Determinants of Demand

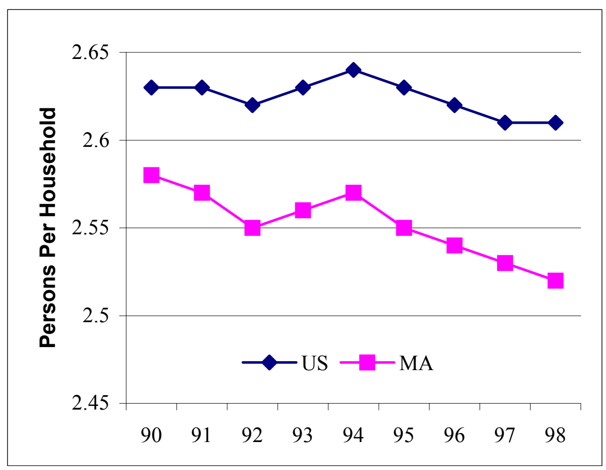
While the supply of housing has remained relatively constant in recent years, demand has increased. Some of the increase in demand is due to the strength of the economy, but a change in household formation has also played a part. Over the last 60 years, the fraction of households made up of one person has consistently grown. As Figure 9 illustrates, the increase in single person households in Massachusetts has been slightly larger than the trend in the rest of the country.

Figure 9: Single Person Households as a Percent of Total Households, 1940-1990



Source: 1940-1990: U.S. Census. 2000: The Joint Center for Housing Studies at Harvard University

Figure 10: Average Household Size, 1990-1998



U.S. Census Bureau, Household and Housing Unit Estimates, <www.census.gov/hhes/www/housing.html>

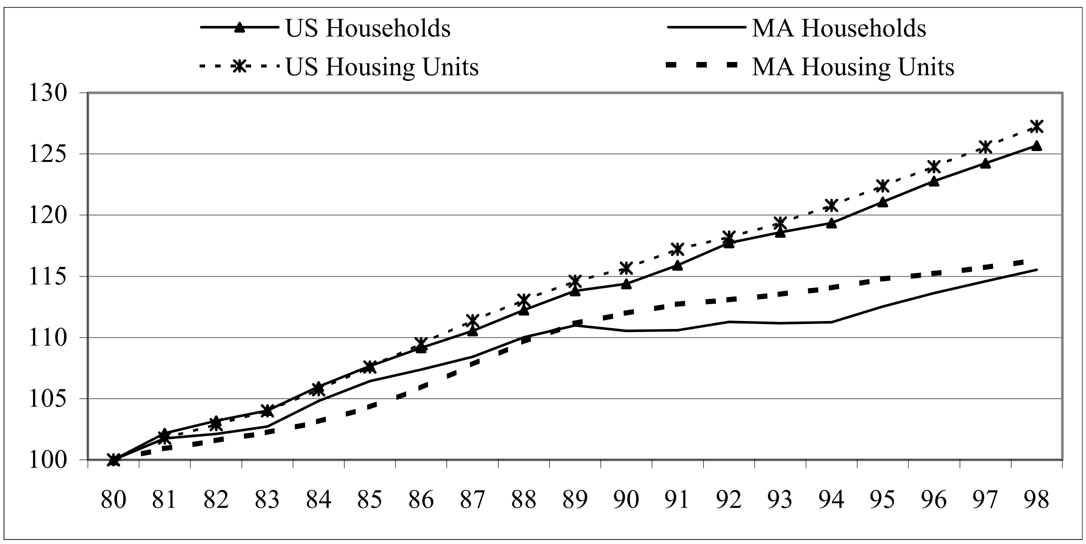
Average household size has been dropping in both Massachusetts and in the rest of the country. The growth in the number of single person households accounts for a large part of this decrease. The decrease in household size has led to a large increase in the number of households since 1980 while there has been only an 8% increase in population.[19] Between 1990 and 1998, Massachusetts' population grew by 2.2%, but the number of households in the state grew by

[19] Another phenomenon since 1980 has been the steady growth of what the census bureau calls non-family households – from 29% in 1980 to 34% by 1996. This accounts for some of the decline in persons per household. Moreover, only 40% of households formed between 1980 and 1996 were 'family' households.

4.4%, twice as fast. The growth in the number of households combined with a decreasing average household size explains some of the increased demand for housing units, even as population growth in Massachusetts has remained low.

As seen in Figure 11 below, during the boom in the 1980's, the number of housing units in Massachusetts grew at a rate faster than the number of households. Since 1989 housing units have continued to grow, albeit at a slower pace than during the rapid expansion of the '80s. The growth in the number of households in the Commonwealth stagnated during the economic slowdown of the early '90s but has taken an upward turn since 1994. Between 1994 and 1998, the number of households in Massachusetts increased by 3.9%, nearly twice the 2% by which the number of housing units expanded during the same time. As has been noted previously, building permits for new residential construction were only slightly higher in 1999 and 2000 than they were in 1998. Housing growth in Massachusetts appears to be relatively unresponsive to changes in the number of households, and in recent years, it has been unable to keep up.

Figure 11: Households and Housing Unit Growth in Massachusetts and the U.S., 1980-1988

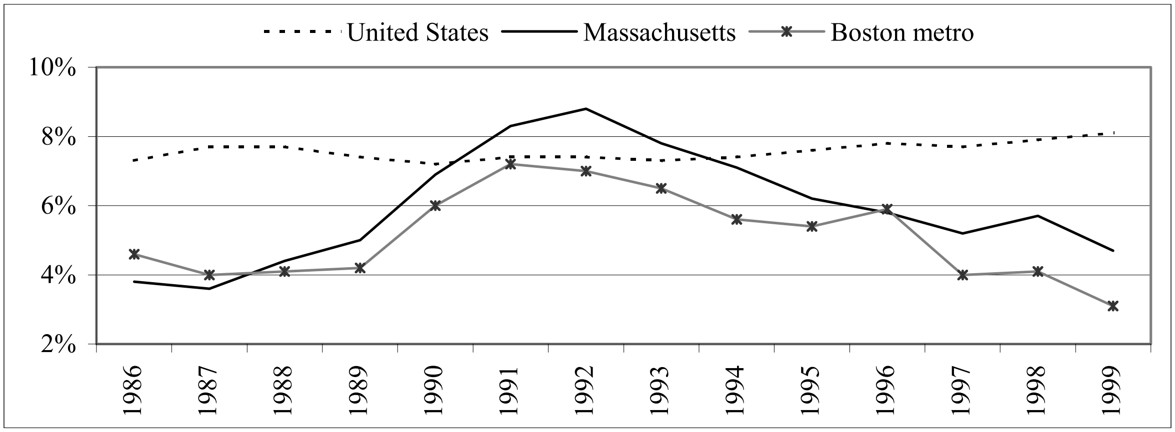


Source: U.S. Census Bureau, Household and Housing Unit Estimates, www.census.gov/hhes/www/housing.html

The increase in demand for housing, coupled with a relatively constant supply, has led to a decline in the vacancy rate. The vacancy rate in Massachusetts has been more volatile than in the nation as a whole. Vacancy rates in the Commonwealth rose sharply between 1987 and 1992. Since 1992, the vacancy rate in Massachusetts has declined from 8.2% in 1992 to 4.7% in 1999. The vacancy rate trend in the Boston Metropolitan Area parallels the state as a whole, though Boston tends to have a lower level of vacancy. The Rental Housing Association (RHA) estimates that the current vacancy rate in Boston is only 1.5%.[20] The decline in vacancies puts upward pressure on rents.

[20] Interview with Edward Shanahan, CEO of the Greater Boston Real Estate Board, August 2000. This number is based on anecdotal evidence from their members' properties.

Figure 12: Vacancy Rates in Rental Housing, 1986-1999

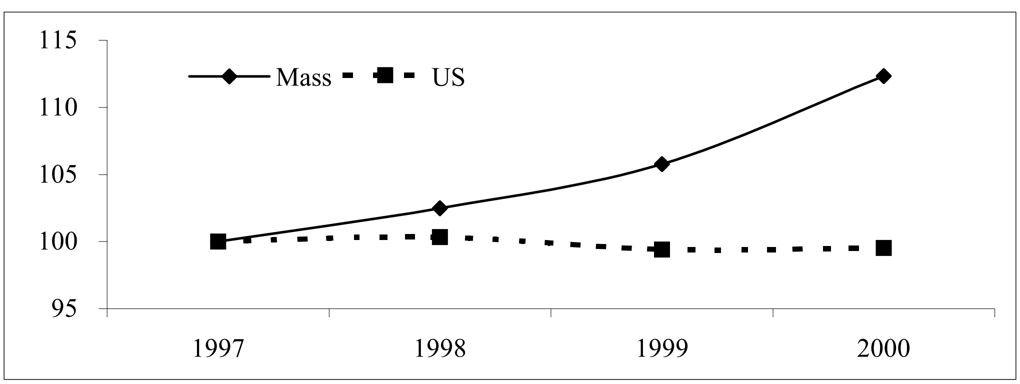


Source: U.S. Census Bureau, Housing Vacancies and Homeownership, www.census.gov/hhes/www/hvs.html>

Impact of High Housing Costs

Massachusetts residents have family, household, and per capita incomes well above the nation's. However, a significant portion of the state's relative income advantage is offset by the state's high cost of living, the most significant distinguishing component of which is the high cost of housing. As Figure 13 shows, the ratio of the median home price to income is rising in Massachusetts while it is flat in the nation as a whole. Between 1997 and the second quarter of 2000, per capita income rose faster in Massachusetts than in the rest of the country. However, while income and home prices rose at the same rate in the United States as a whole, median single-family home prices rose 12% faster than income in Massachusetts. The high price of housing has consumed a significant portion of the income gains for Massachusetts households that were not already homeowners at the beginning of the 1990s.

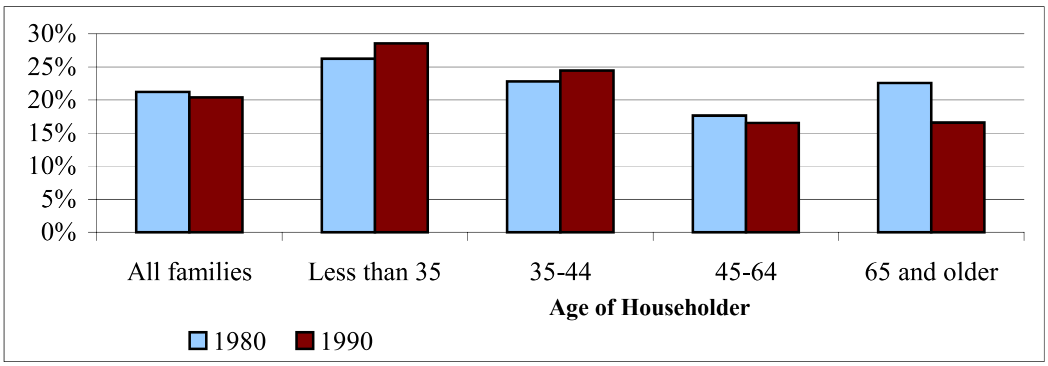
Figure 13: Ratio of Median Single-Family Home Price to Income Per Capita Relative to 1997, 1997-2000



Sources: Housing Prices: U.S. -- National Association of Realtors, <nar.realtor.com>, MA -- Banker & Tradesman, <www.thewarrengroup.com>, Income Data: U.S. Census Bureau Current Population Survey and New England Economic Project

Rapid increases in housing prices create differences in cost burden across age groups. As of 1990, family householders in Massachusetts over the age of 45, many of whom purchased houses prior to the price increases of the 1980s, had the 5th lowest housing cost burden in the United States. Households in Massachusetts in which the householder is less than 35 years old have the 5th highest cost burden in the nation.[21] Continuing price increases in the course of the 1990s would indicate that this pattern of distribution, with high housing cost burdens concentrated among more recent buyers, has likely continued. The implications of this differential are significant, as the high cost of living in Massachusetts hurts its economic competitiveness as businesses and work-age residents choose to locate elsewhere. Rising house prices disproportionately affect young residents between the ages of 25 and 34, who made up 57% of the 220,000 people who have left the state between 1990 and 1997.[22] This exodus of work-age families has slowed the labor force growth and, when combined with the low unemployment rate in Massachusetts, threatens the state's ability to sustain economic growth.

Figure 14: Rent Burden by Age, 1980 and 1990



Source: U.S. Census Bureau

The housing cost burden (the portion of income that must be devoted to housing costs) in Massachusetts is particularly acute for low-income families, especially renters. This would naturally be true in any expensive housing market, but there are indications that recent years may have seen the burden grow heavier for some households.

Both rent and housing prices are rising at rates faster than general inflation. From 1995 to 1999, the rent component of the consumer price index for the Boston-Worcester-Lawrence Consolidated Metropolitan Statistical Area increased by 17.7 %, while the index for all items grew by 11%.[23] (Rents had stagnated or in some areas even fallen during the early part of the 1990s.) This is consistent with recent data at the national level that shows that the price of housing has risen at more than twice the rate of overall inflation and rent at more than one-and-a-half times that rate between 1997 and 1999.[24]

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[21] Sum, Andrew M., Anwiti Bahuguna, Neeta P. Fogg, W. Neal Fogg, Paul Harrington, Sheila Palma, and W. Paul Suozzo, *The Road Ahead: Emerging Threats to Workers, Families, and the Massachusetts Economy*, Massachusetts Institute for a New Commonwealth (1998), p. 88.

[22] *The Road Ahead*, MassINC (1998), p. 100

[23] U.S. Bureau of Labor Statistics

[24] *The State of the Cities 2000*, U.S. Department of Housing and Urban Development (March 2000), p. 50

Serious housing problems, or "worst case needs" – as defined by HUD's classification of households earning less than 50% of the median area income who are paying more than half of their income for housing or live in severely inadequate housing – are increasing nationwide at a faster rate than they have in the past. Between 1991 and 1997, worst case needs households in the United States increased by 12% while the total growth in the number of households only increased by 7% during that same time period.[25] A similar tend has been observed in Massachusetts. According to the 1990 Census, there were 152,000 very low-income[26] renter households with worst case needs in Massachusetts and almost 59,000 very low-income homeowner households who met the same criteria.[27] Within Metropolitan Boston alone, there were 83,000 worst-case needs households.[28] Since then, the number of severely rent-burdened tenants has increased. In 1990, 191,300 Massachusetts renter households paid more than half of their income for housing. In 1998, that number had risen to 241,900, a 21% increase.[29] Rising rents have outpaced the incomes of renters at the bottom end of the income scale.

Increasing the state's housing supply is the first step necessary to ease the upward pressure on housing prices and increase the affordability of housing. Further housing growth is also a necessary component to increase Massachusetts' labor force and ease the state's tight labor market. Low interest rates in the past few years may have masked rising home prices, as mortgages payments remained stable even as home prices surged. Low interest rates cannot, however, be relied on to maintain some degree of affordability. It is critical to allow the market to increase the amount of new housing supplied to better respond to demand.

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[25] *The State of the Cities 2000*, U.S. Department of Housing and Urban Development (March 2000), p. 56

[26] Very low-income households are defined as those households with incomes less than 50% of the median area income.

[27] Analysis by CHAPA.

[28] U.S. Department of Housing and Urban Development, <www.hud.gov/pressrel/worsetab.html>

[29] U.S. Census Bureau, American Housing Survey

The Economics of Housing

An analysis of the economics of housing provides insight into the causes of and potential solutions to the housing shortage; to develop effective policy, the origins of the increase in prices must be understood. During the late 1990's, several factors contributed to an increase in the demand for housing in Massachusetts. The most important factor was the strong economy. In recent years, average personal income has increased at a rate of almost 7% annually in Massachusetts, much faster than the average in the rest of the country. The strong growth in income stimulated the demand for housing. Demographic changes also contributed to the demand for housing. The number of households in Massachusetts is growing at approximately twice the rate of population growth in the state, due to the continuing shift toward smaller households during the 1990's.[30] With fewer people living in each house, even a constant population requires more housing.

When demand for a good increases, economic theory predicts that both the price and quantity will increase. The responsiveness of supply to an increase in demand will determine how high prices will rise. An inelastic supply means that production will not increase, and prices will rise considerably. A more elastic supply will result in a greater adjustment in quantity and less of an increase in price. Academic research into the elasticity of housing supply has not reached a consensus. Studies indicate that housing supply is elastic with respect to price, though elasticity estimates range from 0.3 to 13.[31] The recent increase in demand for housing in Massachusetts has led to a large increase in prices, but little increase in housing production – the symptoms of an inelastic supply. To understand why prices are increasing so quickly, we must ask why the supply of housing is inelastic.

The fact that a unit of housing is tied to a particular location contributes to many of the problems associated with the housing market. The scarcity of available land can constrain growth in housing and contribute to the inelastic supply. There are many reasons why land may not be available. In some communities, there is little undeveloped land. Many towns in Massachusetts have been in existence for hundreds of years, and the amount of land suitable for construction is limited. In many communities however, developable land exists, but government policies restrict the amount of available land that can be developed and the density at which it can be developed.

These restrictions have a severe impact on the housing market. According to Anthony Downs, an economist with the Brookings Institution, "the restrictive behavior of local governments – expressed through their various regulations – is by far the most important single cause of high housing costs."[32] Downs attributes over half of the cost of building new housing to local regulations that are in excess of minimum requirements for health and safety. Others find lower but still substantial effects. A federally convened commission on regulatory barriers to

30 In recent years, the population in Massachusetts has increased by less than 0.5% each year, while the number of households grew at a rate of 0.94% on average between 1994 and 1998.

31 DiPasquale, Denise, *Why Don't We Know More About Housing Supply?,* University of Chicago (December 1997). Some of the range is explained by the fact that different studies examine different time periods; one would expect supply to be more elastic in the long run.

32 Turner, Margery Austin, and G. Thomas Kingsley, "*Housing Markets and Residential Mobility*" The Urban Institute Press (Washington, DC, 1993), p. 261

affordable housing reported in 1991 that "the Commission has seen evidence that increases of 20 to 35 percent in housing prices attributable to excessive regulation are not uncommon."[33] William A. Fischel of Dartmouth College found that growth controls raise housing prices by 8% to as much as 38%.[34]

Local governments intervene in the housing market and restrict growth for many reasons. One reason is the impact that new development has on local residents. New housing may change the character of a city or town and generate increased traffic congestion and pollution, which will often be opposed by local residents. It will also alter the value of existing property. Because the value of a house is related to the characteristics of the surrounding neighborhood, local homeowners benefit if their community only allows builders to construct new housing that is more valuable than the existing properties, thereby restricting growth of low and moderately priced housing. They may also benefit by stopping or limiting development more generally to restrict the supply of housing and force prices up. Existing homeowners will often support restrictions and barriers to development to preserve their quality of life and to increase the value of their homes. But prospective homeowners and renters, who remain exposed to housing price increases, suffer the consequences.

Local Concern About Increased Municipal Cost Burden

Zoning rules not only have the support of local residents, who would like to increase the value of their homes and prevent congestion, but they also are promulgated by local officials, who respond to the desires of their constituents and who wish to minimize the pressure on local budgets that can result from new residential development. Thus, zoning rules and restrictions on new housing are often much more stringent than an efficient market would require.

New development places additional burdens on local government. According to University of California at Berkeley professor Elizabeth Deakin, local officials throughout the nation share the fear that residential development will cost communities more than they can collect in taxes.[35] Massachusetts housing agencies, including the Department of Housing and Community Development, the Massachusetts Housing Finance Agency, and the Massachusetts Housing Partnership Fund report that this concern figures prominently in a majority of cases where there is local opposition to housing development. Representatives of the residential development community convened in conjunction with the preparation of this report agreed that municipal cost concerns were a significant factor in opposition to proposed development projects. That session was not the only occasion on which they expressed this view. "'The philosophy being applied is that new people cause new schools, so let's keep new people out of town,'" J. Owen Todd, a lawyer for the Greater Franklin Developers Association, told the *Boston Globe*.[36]

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[33] The Advisory Commission on Regulatory Barriers to Affordable Housing, "*Not in My Back Yard: Removing Barriers to Affordable Housing*" Report to the President (1991), p. 1-1

[34] Fischel, William A., "*Do Growth Controls Matter? A Review of Empirical Evidence on the Effectiveness and Efficiency of Local Government Land Use Regulation*" Lincoln Institute of Land Policy (1990), p. 33

[35] Fischel (1990)

[36] "*Court Rules Against Franklin School Fees*" The Boston Globe (June 27, 2000), p. B1

Research indicates that this local concern about municipal cost burden is justified for at least some types of residential development. Studies by The American Farmland Trust and Commonwealth Research Group, Inc indicate that for every dollar of property taxes generated, residential development consumes between $1.02 and $1.16 in local services.[37]

The primary municipal costs that increase as a result of residential development are school costs. This is because new residential development often means more school children, whose education costs cannot always be offset by the property tax revenues generated by the new development. Communities fear not only that more schoolchildren will increase operating costs in the short term by requiring more teachers and supplies, but also that in the long term, enrollment growth will require the expansion of existing schools or the construction of new ones. Increases in school costs are important to communities, because school spending makes up a major portion of their budgets. In fiscal year 1998, school expenditures constituted 48.7% of all municipal spending in Massachusetts, and the median percentage of local spending devoted to schools was 54.8%.

Developers hoping to gain local approval of projects commonly propose housing units of one or two bedrooms, often restricted to the elderly, to assure communities that their proposed developments will not increase school enrollment.

In a model generated by the Executive Office for Administration and Finance (EOAF), new residential single-family development in Massachusetts only generated enough tax revenue to cover the educational and other costs incurred by the municipality as a result of that development once the assessed value of the property reached approximately $215,000.[38] A fiscal impact study performed in January 2000 by Connery Associates and Community Planning Solutions for the City of Leominster is consistent with analysis by EOAF. It finds that taxes generated by existing residential development do not cover the municipal costs of development until the assessed value of the property reaches approximately $150,000. For new residential development, the value at which the development becomes revenue-neutral is $225,000.

To illustrate the costs associated with new development, the following example isolates the effect that additional schoolchildren will have on town finances. The 1987 American Housing Survey conducted by HUD found that each additional unit of single-family housing resulted in an average of 0.7 additional school-age children.[39] Analysis by the Executive Office for Administration and Finance indicates that on average, a new single-family house developed in Massachusetts between 1993 and 1998 was associated with 0.49 additional students in the community's school system. After factoring out the tax assessment on a home with an assessed value of $150,000, and the additional state aid each new student can be expected to generate, every additional single-family home could cost a community approximately $800 in unrecovered education expenses alone.

[37] The American Farmland Trust, "*Does Farmland Protection Pay? The Cost of Community Services in Three Massachusetts Towns*" (1992); Commonwealth Research Group, "*Cost of Community Services in Southern New England*" 1995

[38] In 1998, approximately one half of single-family houses built in Massachusetts fell below this cost threshold.

[39] The Commonwealth of Massachusetts Department of Housing and Community Development, "*The Growth Impact Handbook: Ways to Preview Your Community's Future*" (1998), p. 57

Table 3: Additional Education Expenses Associated with Single-family Housing Development

For Illustrative Purposes Only

Average Annual Education Cost Per Pupil in the Commonwealth	$7,000
Additional Pupils Due to a New Single-family Unit	0.49
Expected Additional Education Expense Due to a New Single-family Unit ($7,000 * 0.49)	$3,430
Less: Anticipated Tax Revenues From a $150,000 Home (0.017 Average Property Tax Rate * $150,000)	$2,550
Less: Additional Education Aid From New Students – Assuming District is Above Foundation ($150 Required Minimum Aid * 0.49)	$74
Annual Unrecovered Education Costs for a New Single-family Housing Unit	$806

Cities and towns at the foundation funding level[40] will receive more state aid for each additional student, but they will also be less wealthy and have lower anticipated tax revenues per unit. Moreover, the above calculation does not take into account the costs of funding non-education services for the community's new residents, such as new roads, sewers, and public safety.

Local Barriers to Housing Production in Massachusetts

Nationally, barriers to residential development take two general forms: 1) ordinances requiring inflexible construction standards and minimum structure sizes and 2) ordinances requiring low residential densities. Localities can also passively restrict development by making it difficult, time consuming, or costly to acquire permits. Research by Anthony Downs and by the Advisory Commission on Regulatory Barriers to Affordable Housing established by the United States Department of Housing and Urban Development (HUD) in 1990 indicates that local ordinances often mandate standards for new development that are well in excess of those under which most of the country's homes were built. Most suburbs in the United States prohibit residential densities in excess of 10 units per acre even though many parts of the country have high quality housing at densities of more than 35 units per acre.[41] At the end of the last decade in King's County, Washington – which was, and still is, one of the hottest real estate markets in the

[40] The foundation funding level is the minimum level of educational funding per student required by the Education Reform Act of 1993.

[41] Turner and Kingsley (1993), p. 262

country – more than 1,500 square miles of land were zoned to allow only one house per every five acres of land.[42] Of the 155 Massachusetts communities analyzed by the Executive Office of Environmental Affairs to date, 95 have zoning regulations that, on average, require more than one acre per unit. Four communities average over three acres per unit. Many cities and towns have zoning districts with significantly higher acre per unit requirements than these community-wide averages.

Zoning and Subdivision Control Laws in Massachusetts

"The Zoning Act" was enacted in 1975 to "facilitate, encourage and foster the adoption and modernization of zoning ordinances and bylaws by municipal governments;" and to establish standardized procedures for their administration. The purpose of zoning is to promote the health, safety, convenience and welfare of the inhabitants of a city or town, and specific goals include, but are not limited to, the following:

- to lessen congestion in streets;
- to secure safety from fire, flood, panic and other dangers;
- to prevent overcrowding of land;
- to provide adequate light and air;
- to encourage housing for persons of all income levels;
- to facilitate the adequate provision of transportation, water, water supply, drainage, sewerage, schools, parks, open space and other public requirements;
- to encourage the most appropriate use of land throughout the city or town, including consideration of the recommendations of the master plan, if any, adopted by the planning board and the comprehensive plan, if any, of the regional planning agency; and
- to preserve and increase amenities by the promulgation of regulations to fulfill said objectives.

Cities and towns throughout the Commonwealth have the authority to enact zoning regulations as they see fit addressing the above issues. The Zoning Act gives a municipality the ability to define how it will grow, maintain open spaces, manage traffic and promote a variety of uses to create an atmosphere that encourages residential, industrial and commercial uses. Zoning regulations usually divide the community into various zoning districts by use, thus separating land for residential, commercial and industrial uses. Zoning regulations are generally written to provide the most protection for single- and two-family residential districts, and exclude from these districts uses regarded as incompatible with the residential environment. Multifamily residences are often found in the next tier of uses, and many communities require special permits for their construction. Communities have the authority to place dimensional controls on parcels and buildings. For residential uses, these controls include lot area, setbacks, lot frontage, lot

[42] The Advisory Commission on Regulatory Barriers to Affordable Housing (1991), p. 2-7

coverage, floor area ratio, and building height, and may also address other issues such as buffer zones, parking and signage. These controls often define the personality of a neighborhood.

Subdivision control laws in Massachusetts originated from a concern over the effect of subdivisions on the planning and development of streets within a community. The first comprehensive subdivision control statute was enacted exclusively for the city of Boston in 1891. By 1916 similar powers were conferred on boards of survey in many cities and towns throughout the Commonwealth. When a community establishes a planning board, the Subdivision Control Law is in effect unless the local legislative body votes not to accept the provisions of the law.

While the Subdivision Control Law specifically prohibits a planning board from adopting regulations relating to the size, shape, width, frontage or use of lots within a subdivision, or to the buildings to be constructed on the lots, it nevertheless provides localities with significant authority in the development process. Developers must conform not only with zoning laws but also with the requirements of the local planning board. The list of requirements that planning boards may impose is extensive. Once the Subdivision Control Law is operable in a community, the planning board is required to adopt regulations with respect to the location, construction, width and grades of proposed ways and the installation of municipal services. Planning boards may adopt regulations prescribing the standards for turnarounds and dead end streets, underground distribution systems for utility services including electrical and telephone services, police and fire alarm boxes and any similar municipal equipment, and street lighting. Planning board regulations can also include standards for the orientation of new streets, lots and buildings, building set back requirements from property lines, limitations on the type, height and placement of vegetation and restrictive covenants protecting solar access which are not inconsistent with existing local bylaws or ordinances.

Planning boards also usually prescribe the size, form the content, style and number of copies of plans, and set the procedure for submission and approval of plans. They may adopt regulations requiring a subdivider to submit information relating to dwelling size, type, location and population for purpose of analyzing sanitary and storm sewer systems and water systems. Planning board regulations can also require that a subdivider submit a topographic map showing proposed grades at two-foot contours and an impact statement showing the effect of the proposed development on schools, police and fire protection, traffic patterns and other municipal services, even though the Subdivision Control Law prohibits planning boards from regulating these subjects.

Zoning laws have a dramatic effect. In Massachusetts, developed land now has less than half the population density (4.97 persons/acre) than it had in 1950 (11.19 persons per acre). Between 1950 and 1990, the amount of developed land increased at a rate greater than six times population growth.[43] One of the reasons for this precipitous drop in density is the imposition of regulatory barriers that require significantly more land to build a unit of housing. For instance, many Massachusetts communities require not only minimum lot sizes of an acre or more, but also minimum setbacks for the buildings, minimum front yard area, minimum lot widths, and on-site parking requirements. Accessory, or "in-law," apartments are often prohibited. Forty-five communities in the Commonwealth have adopted explicit growth rate by-laws that limit the

[43] U.S. Census Data, University of Massachusetts/MacConnel Land Use Data, MassGIS Analysis

construction of new units to as little as 50 per year. Of sixteen communities reviewed in depth by the Executive Office for Environmental Affairs (EOEA), six had adopted regulations making it impossible to build multifamily housing in any form.

There are high barriers to entry when it comes to developing real estate in Massachusetts. In fact, some firms use these entry barriers as part of their business strategy. Large firms that can afford to wait and are able to placate or overcome local objections can rely on high entry barriers that keep others from building competing developments and diminishing their high rents and profits. In a recent filing with the Securities and Exchange Commission, AvalonBay Properties, a major national real estate investment trust (REIT) with projects in Massachusetts, says the following:

> We focus on the ownership and operation of upscale apartment communities (which we consider to be apartment communities that generally command among the highest rents in their sub-markets) in high barrier-to-entry markets of the United States. This is because we believe that the limited new supply of upscale apartment homes in these markets helps achieve more predictable cash flows. These barriers-to-entry generally include a difficult and lengthy entitlement process with local jurisdictions and dense in-fill locations where zoned and entitled land is in limited supply. These markets are located in Northern and Southern California and selected states in the Mid-Atlantic, Northeast, Midwest and Pacific Northwest regions of the country.[44]

One way to quantify the extent to which these barriers constrict housing supply is to compare how much new development is allowed on vacant land zoned for residential development to the residential density of developed land within the same community. In the sixteen cities and towns reviewed by the Executive Office for Environmental Affairs, current zoning regulations permit an average development density of 0.9 units per residentially zoned acre compared to the average of 1.8 units per acre that now exists on land already developed in those communities.[45] EOEA data from an additional 139 communities indicate that that allowable density of future residential development also averages approximately 0.9 units per acre. In some towns, new development requires nearly 3.5 times as much of land as existing development, and in only one of the sixteen communities reviewed do current zoning regulations allow density equivalent to the status quo. This means that current zoning regulations require much less efficient use of land relative to existing development, adversely impacting both the cost of land and the environment.

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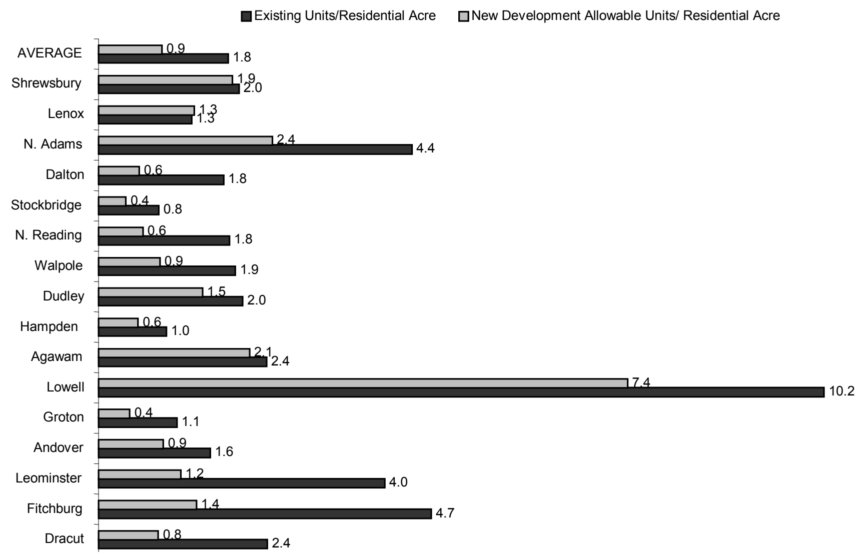
44 AvalonBay Properties 10K filing with the U.S. Securities and Exchange Commission for the year ending December 31, 1999, p. 36. Accessed through the EDGAR database at the SEC's website.

45 Executive Office of Environmental Affairs

Figure 15: Allowable Development Densities



Source: Executive Office for Environmental Affairs

Because restrictive local policies limit development, they have contributed to the run-up in housing prices. Easing the controls would allow the housing supply to respond better to an increase in demand and would slow the rise in prices. However, local governments impose these policies for concrete reasons, primarily to avoid additional strain on their budgets. Attempts to stimulate development will be met with resistance unless they address these concerns and provide additional incentive to allow new construction. In FY 2000, the Administration filed legislation to create the Housing Supply Incentive Program, which compensates communities for a portion of the additional costs associated with new development, thus encouraging them to allow more low and moderately priced housing.

Restrictive local policies not only reduce the amount of land available for development and decrease the number of units that can be built on undeveloped land, but they can also exacerbate the economic stratification of communities. Even without zoning rules, many communities would still be sorted by income. A developer free to decide how many units to place on a parcel of land faces a trade off between building many small units or fewer large units. The profit-maximizing choice will likely vary depending on the location of the land. In neighborhoods characterized by small houses or multifamily housing, buyers will not pay the same premium for a 5,000 square foot house as they would if the house were surrounded by other large houses. Developers will naturally wish to build large houses in more expensive neighborhoods, and smaller houses and multifamily housing in other neighborhoods. To some extent, neighborhoods will become economically sorted unless affordability mandates or other government programs support or require economic integration. Zoning and other restrictions on development will also reduce the number of low and moderately priced houses for two reasons. One, as previously discussed, is that the restrictions often limit development to larger, high-value homes. The second is that where developable land is kept scarce, the financial return on improvement and maintenance of the current housing stock is greater, which means that fewer units filter down to low-income families.

Building and Related Specialty Codes

In addition to zoning and land use controls, local governments also implement other regulations, which affect the cost and timing of development. Among these are the State Building Code and related specialty codes.

The Massachusetts State Building Code (780 CMR) is a uniform, statewide code that contains the minimum standards for the construction, alteration, repair, demolition, and use of all buildings and structures (with the exception of those that pertain to the specialty codes listed below). Chapter 34 of the State Building Code pertains to the repair, alteration, addition, and change of use of existing buildings. The State Board of Building Regulations and Standards (BBRS), which reports to the Secretary of Public Safety through its administrator, promulgates and maintains the Massachusetts State Building Code.

In addition to the State Building Code (780 CMR), Massachusetts has a number of "specialty codes" that contain provisions related to buildings and structures. Included among the state's specialty codes are those promulgated or interpreted by the following boards or agencies:

- Board of State Examiners, Plumbers, and Gasfitters (Plumbing and Gasfitting Codes - 248 CMR);
- Department of Public Health (Sanitary Codes - 105 CMR);
- Board of Fire Prevention Regulations (Fire Prevention and Electrical Codes - 527 CMR);
- Architectural Access Board (Handicap Accessibility Codes - 521 CMR);
- Department of Environmental Protection (e.g., Drinking Water Regulations - Cross-Connections Control – 310 CMR 22.00);
- Board of Elevator Regulations (Elevator Codes - 524 CMR);
- Board of Boiler Rules (Boiler Regulations – 522 CMR); and the
- Department of Telecommunications and Energy.

Conflicting or Duplicative Codes

Many of the codes that regulate building construction, i.e., the State Building Code (780 CMR) and the specialty codes listed above, are independently promulgated by each relevant board and state agency. As a result, the Commonwealth will sometimes put into place regulations that are conflicting or duplicative. For instance, a builder can be in a position where he cannot meet all the requirements of one state code without violating the provisions of another. In addition, some codes are duplicative, meaning that they include the language of other codes.

As a result, builders trying to comply with the Commonwealth's regulations sometimes face multiple local officials enforcing rules promulgated or inconsistently interpreted by multiple state government jurisdictions. This may result in builders complying with the more restrictive and perhaps more costly interpretation. For the most part, the conflicting or duplicative codes may be inadvertent and due to the large number of regulations and statutes encompassing these areas.

Inconsistent Interpretation and Enforcement of Codes

Although it is the Commonwealth's responsibility to promulgate the building and specialty codes, local building and fire prevention officials and local plumbing, gas, electrical, and health inspectors are responsible for the interpretation and enforcement of these regulations. Discussions with builders, architects, and state regulators indicated that local officials throughout the Commonwealth sometimes impose building requirements that are both unduly restrictive and in direct violation of state regulations. Although most local officials have good intentions, unduly restrictive building requirements drive the cost of housing upward.

Without knowledge of the basis for these regulations, some local officials impose additional requirements that they believe will promote public safety. This lack of understanding by local officials can also result in the misinterpretation of state codes. In addition, while most local officials are skilled at identifying code violations after a building has been constructed, some officials are not fully trained in reading architectural and engineering plans and, therefore, cannot effectively identify code violations within those plans. This results in an inability among some local officials to expediently recognize code violations within a building's plans prior to the building's construction. As one would expect, bringing an element of a new or rehabilitated building up to code after its completion is usually much more costly than effectively planning for code compliance prior to construction.

When a local inspector or safety official makes determinations that a builder or tradesperson believes to be incorrect, or if a local official does not act expeditiously, there is often no practical recourse. Because builders and sub-contractors working in a community must rely on local officials to approve their future work, they are reluctant to make complaints or appeals. Property owners similarly acquiesce rather than seek redress so as not to imperil future approvals of their specific projects.

While processes surrounding the enforcement of building and related specialty codes pose one set of impediments to housing development, another set of impediments arise from formally-imposed requirements that are beyond the locality's authority. For example, localities sometimes impose building requirements (as opposed to site requirements) through their approval process under the Subdivision Control Act (see page 21), though they are not legally permitted to do so.

Title 5

Discussions with representatives of the residential development industry indicate that another source of expense and delay in housing development is caused by the local variations in the enforcement of Title 5 (310 CMR 15), the state regulation governing on-site subsurface sewage systems, including septic systems. The state Department of Environmental Protection (DEP) revised Title 5 of the State Environmental Code in 1995 to provide greater protection for certain sensitive resources, including drinking water, than had been provided by the 1978 code. The requirements included in the 1995 Title 5 update were found to be scientifically valid and necessary to the protection of public health and the environment in the process of developing the code revisions.

Title 5 calls for existing systems to be inspected before property is transferred and, if they fail, to be upgraded within two years. New construction must also comply with the stricter protection standards. To improve the siting and design of systems, the 1995 code contains more comprehensive requirements for site evaluations and requires a DEP-approved soil evaluator to evaluate the soils on a site. To increase protection of groundwater resources used for drinking water supplies, the 1995 code also designates nitrogen-sensitive areas. In nitrogen-sensitive areas, the 1995 Title 5 code limits the maximum design flow of septic systems to 440 gallons per day (the typical design flow for a four-bedroom house) on a one-acre lot . As a result, a one-acre lot is normally required for a four-bedroom house and a three-quarter acre is usually required lot for a three-bedroom house not served by a sewer in a nitrogen-sensitive area. The use of approved "innovative and alternative" (I/A) treatment methods can allow the construction of a house with more bedrooms than might otherwise be permitted on a particular site or the construction of a house on a smaller site than might otherwise be allowed.

Local boards of health are the primary enforcement and regulatory authorities under Title 5, though DEP is involved in approving certain alternative technology and variance requests. Recognizing that there are varying conditions across the state, the code allows communities to establish local bylaws that are more stringent than Title 5, and DEP is aware of 125 communities that have done so. Such stricter requirements may be appropriate to deal with specific local conditions. On the other hand, a community wishing to restrict residential development could effectively do so, or at least make it more expensive, by adopting excessively strict requirements for septic systems. In addition, a local board of health might adopt an unnecessarily tight standard as a result of an inaccurate analysis of conditions or technology. DEP indicates that some communities may have adopted local bylaws more stringent than Title 5 that may not have their foundation in science. Examples of such bylaws slow development, add to its cost, or unnecessarily prevent any development on certain lots by:

- Not allowing the use of alternative and innovative technologies approved by DEP
- Requiring soil absorption systems than can handle 200% of the required design flow
- Requiring greater setbacks to wetlands than Title 5 requires
- Not allowing soil to be mounded to accommodate a septic system
- Allowing soil evaluations only during certain parts of the year (e.g. during the last two weeks of April or the first two weeks of May)
- Requiring a *minimum* 12-foot separation between leaching trenches in all systems, while 12 feet is the *maximum* separation required in Title 5
- Contrary to Title 5, not allowing the space between leaching trenches to be used as "reserve areas," thereby increasing by 200% the amount of land that must be used for a system.

In addition, certain processes may use Title 5 to further impede development by making it more costly. For example, only installers certified by the board of health may install a septic system in a community, which must then be inspected by a separate inspector. This limits a property-owner's choice of contractors to install a septic system, reducing competition and potentially driving up cost.

Developers contend that, in addition to the expense required by the basic requirements of Title 5, the variation in local application and the existence of additional local standards have imposed direct costs, as well as uncertainty and delay that have significant costs of their own. The result is that an environmental protection code intended primarily to protect water supplies can be misused to restrict land use.

Federal and State Interventions in the Housing Market

Local governments are not the only ones that intervene in the housing market. Both federal and state governments also play a role in the housing market. Some policy decisions impact the housing market directly (such as subsidies for production and rent support, as well as the preferential tax treatment of mortgages), while other policies have an indirect impact (such as environmental regulations and programs that preserve open space). Much state and federal intervention is designed to provide affordable housing, and it often works at cross-purposes with local policies. For example, the state and federal governments subsidize low-income housing, a type of development that communities often wish to keep out.

In contrast to local government intervention in the housing market that often limits development, many federal and state policies are aimed at assisting low-income families. Affordable housing policies usually fall into one of three categories: demand-side approaches, supply-side approaches, or regulatory approaches. Each of these types of intervention is meant to improve the access to housing for low-income families or individuals, but they work in different ways. Theoretical models of the housing market predict that the consequences of these policies will be quite different.[46]

Demand-side policies usually involve subsidies to low-income renters. These subsidies redistribute income from taxpayers to recipients. This type of policy will directly improve the welfare of recipients, although it can have the unintended consequence of increasing rents and negatively affecting non-recipients. Because these subsidies directly raise the incomes of these families that receive them, they have the indirect result of raising demand for rental units. The higher demand should also stimulate construction of rental units. However, if the supply of housing is restricted, subsidies by themselves cannot alleviate a housing shortage. Empirical research into the effects of demand-side approaches yields mixed results. Analysis of the first experiments with tenant-based subsidies in Green Bay, Wisconsin and St. Joseph County, Indiana -- the precursors of Section 8 certificates and vouchers -- produced competing studies. Rydell (1982) estimated that increased demand created by the tenant subsidies stimulated supply in the short-run, while Weicher (1990) found no evidence of additional housing construction.[47]

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[46] This discussion stems from Rothenberg, Jerome, George C. Galster, Richard V. Butler, and John Pitkin's "*The Maze of Urban Housing Markets*" The University of Chicago Press (Chicago 1991)

[47] Rydell, Peter C., "*Price Elasticities of Housing Supply*," The Rand Corporations, R-2846-HUD (September 1982), Weicher, John, "*The Voucher/Production Debate*," in Denise DiPasquale and Langley C. Keyes, *Building Foundations: Housing and Federal Policy*, (Philadelphia, PA: 1990)

Supply-side policies often offer subsidies for the construction or renovation of low-income housing. The impacts of this type of subsidy are more difficult to gauge and depend on the exact nature of the policy. Construction subsidies increase the production of low-income units, but in low-demand markets they can also result in the abandonment of some low-quality housing stock as demand is siphoned off into new units. Murray's (1983, 1994) analysis of direct supply-side incentives indicates that such programs can displace private housing.[48] He found that three-quarters of public housing units represented additions to the housing stock while one-quarter displaced private construction. Murray also concluded that subsidized private housing, which he termed moderate-income housing, replaced unsubsidized construction and added little to the total housing stock. Programs that reduce the cost of capital to investors, such as tax credits, however, do seem to stimulate production. According to DiPasquale and Wheaton, a one percentage point decrease in the cost of capital for investors increases rental housing production by 14%.[49] In addition to the possible displacement of existing property, supply-side policies have an additional shortcoming: if a subsidy requires the provision of units at below-market rents, landlords have little incentive to maintain the property. The benefits of the subsidies will therefore be eroded over time as the units deteriorate. Finally, subsidies can also contribute to the concentration of low-income housing in one neighborhood.

Regulatory efforts to aid low-income residents include regulations such as affordability mandates, which require builders to include less expensive units in new construction. These policies effectively impose an additional cost on developers who wish to build middle and upper-income housing. They have a similar effect as subsidies for production of low-income housing, although in this case middle and upper-income buyers bear the cost rather than the taxpayers. One advantage of this type of policy is that it can result in a more economically diverse neighborhood, but it may also discourage development.

While the unintended negative consequences of such policies may hurt low-income families, some advocates of government intervention argue that the housing market is inherently unable to serve the needs of the poor. As Howard Husock of the Kennedy School of Government observed, "the belief that the private housing market will victimize the poor, rather than serve them, is deeply ingrained in American public consciousness."[50] While the housing market is unlikely to produce housing for the very poor, it can produce housing that is affordable to people with low incomes that is in some ways superior to public housing. As an example of the market's ability to serve low-income consumers, Howard Husock describes the emergence of three-decker houses in New England during the last century. Three-decker houses permitted lower-income families to purchase property and rent the remaining two units to tenants to help defray the mortgage cost. The houses provided both low-cost entry into homeownership and low-rent housing. Also, in contrast to public housing, resident-owners have the incentive to maintain the properties. The three-deckers housed hundreds of thousands of low-income people at low cost with no government support. However, by the 1930's town zoning ordinances had effectively ended the construction of three-deckers. These ordinances were passed for a number

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48 Murray, Michael P., "*Subsidized and Unsubsidized Housing Starts: 1961-1977*," Review of Economics and Statistics, LXV(4), (1983), p. 590-597, and Murray, Michael P., *"Subsidized and Unsubsidized Housing Stocks: Crowding Out and Cointegration,"* mimeo (1994)

49 DiPasquale, Denise, and William C. Wheaton, *Urban Economics and Real Estate Markets*, Prentice Hall (Englewood Cliffs, NJ: 1996)

50 Husock, Howard, "*Rediscovering the Three-Decker House,*" The Public Interest (Winter 1990), p. 49

of reasons, including worries about fire hazards and the desire in some towns to keep immigrants out. Whatever the reason, in this case government intervention arguably made it more difficult for low-income families to find housing and contributed to the problems we face today. In the 1980s the city of Boston reversed this course and began a program to build three-deckers on vacant lots to alleviate its housing shortage. However, that small program was the exception, and even in Boston many barriers still prevent the market from creating low-income housing.

The development of three-deckers is an example of new construction that served low and moderate-income households. However, much low-income housing comes not from new construction but from a filtering process that takes place in the existing housing stock. Even relatively expensive development can benefit low-income residents. When an expensive unit of new housing is built, the buyers of the unit may move out of a unit that they find less desirable. The newly vacant unit could then be sold to another family, which would again leave a unit vacant. This process could continue over time until low-income households are able to move into better-quality units.

Housing as an Investment

Housing has a unique set of characteristics that distinguish the housing market from other markets. One of the unusual characteristics is that housing both provides a service and functions as an investment. The dual functions of housing influence market outcomes. Investment and consumption decisions are based on different motivations and can therefore lead to different outcomes. Homeowners may choose to improve properties and landowners may build on their property even when prices are low. At the same time, even in areas with high housing prices, it can be rational for property owners to maintain undeveloped land. Landowners who expect the price of housing to increase may wait to build or hold the undeveloped land as an asset.

The fact that property is an investment can also lead to speculation and volatility in the market. According to a survey by Karl Case and Robert Shiller, expectations of continued price increases play a significant role in driving demand for housing.[51] When prices are increasing, everyone "knows" that buying property is a good investment. This type of speculation can lead to larger swings in price than would occur if demand were driven only by the demand for housing services. Boston in the 1980's provides an example of the possible consequences of speculation. Housing prices increased by almost 40% per year, well above what could be explained by changes in fundamentals. As Karl Case and Leah Cook discuss, such rapidly changing housing prices have a large impact on the distribution of real income and wealth.[52] Rising home prices benefit homeowners at the expense of non-owners. Because high-income households are more likely to be homeowners, a boom in the housing market widens the gap between the rich and poor. It will also negatively affect the younger generation, who will face higher real housing costs and a lower probability of owning their own homes. Prices in recent years have not increased as fast as they did in the 1980's, but the distributional consequences are still likely to be substantial.

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[51] Case, Karl E., and Robert J. Shiller, "*The Behavior of Home Buyers in Boom and Post-Boom Markets*" New England Economic Review (November/December 1988), p. 29-46

[52] Case, Karl E., and Leah Cook, "*The Distributional Effects of Housing Price Booms: Winners and Losers in Boston, 1980 –88*" New England Economic Review (May/June 1989), p. 3-12,

A Statistical Analysis of Housing Production in Massachusetts

Recently, fewer than 19,000 housing permits have been issued in Massachusetts each year. Most of these permits have been for single-family houses; single-family housing production makes up 82% of the housing built in the state, compared to 75% for the nation as a whole. The number of single-family permits pulled in 1999 was actually 8% lower than the number pulled in 1994. While almost every community in the Commonwealth experiences some single-family housing production on an annual basis, there is a fundamental difference in the amount of development that has occurred in Eastern and Western Massachusetts. Of the top 100 communities ranked by number of single-family permits, only six communities are located in Western Massachusetts. Within the top 10% of communities, there is a heavy representation of communities on the Cape, in Southeast Massachusetts, and in I-495 communities.

Construction of multifamily housing is much more concentrated than that of single-family housing. While only three communities in Massachusetts have no existing multifamily parcels, less than 50% of the 351 communities issued multifamily permits between 1997 and 1999. The multifamily construction that exists occurs primarily in Boston, which is home to 22% of the multifamily permits pulled between 1997 and 1999 and 40% of those pulled in 1999. Other eastern urbanized areas such as Lawrence, Quincy, Braintree, as well as a few suburban areas like Tewksbury, Ashland, and Yarmouth are also home to multifamily developments.

Municipal Costs of Residential Development

There is a large body of evidence that local government policies restrict the supply of housing and increase housing prices, and economic theory offers several explanations for these restrictions. As discussed previously, one possible reason that communities limit growth is the burden it places on local budgets; the Housing Supply Incentive Program is specifically designed to ease this burden. A statistical analysis can test whether consideration of the financial burden explains some of these growth controls, and by extension, whether the Housing Supply Incentive Program addresses a key problem.

Unfortunately, it is very difficult to quantify the many local policies that affect housing markets. Zoning ordinances vary from town to town, but not in ways that are easy to measure. Nevertheless, statistical analysis can provide some insight into the limits communities place on development. Although local policies themselves are difficult to measure, data on the number and type of permits issued should reflect local constraints.

Between 1997 and 1999, 348 out of 351 communities in Massachusetts issued at least one residential permit. The number of units that cities and towns issued permits for in one year ranged from zero to 1,028, with an average of 54 units each year.[53] Only 141 municipalities issued permits for multifamily housing, and seven of them account for half of all the multifamily units permitted.

[53] Data for some communities was not available for 1999. For those communities, only data from 1997 and 1998 were used.

Any statistical analysis must control for other factors that might influence the number of units permitted. The number of housing permits issued in a community will be affected by both demand and supply. Factors that affect the desirability of a community influence the demand for housing: location, rural/urban setting, density, traffic congestion, school quality, and perhaps other characteristics, as well as home prices. Other factors that influence housing demand include characteristics of the buyers themselves: income, age and birthrate, and population. Supply will be determined by the amount of available land, a community's willingness to allow development, production costs, and home prices. A community's willingness to make land available and allow development can be shaped by many of the same factors that influence demand: income and wealth, age, population density, urban/rural setting, and the price of a home.

The overlap between characteristics that impact supply and demand makes it difficult to predict the effect of many of the control variables. Wealthy communities could have higher demand for homes, but at the same time prices will likely be higher and the community may be more resistant to development. The ultimate effect of wealth or income on the number of permits is an open question. Similarly, a high population density could indicate pent-up demand for housing but at the same time it may make the community less attractive. A rural community may have more land available and lower prices, but it may also offer fewer amenities and job opportunities than an urban community.

The analysis begins by regressing the natural logarithm (log) of the average number of residential units permitted each year on a set of control variables.[54] The demographic controls include the population, population density, median income, average age, and birthrate. The community controls include the number of existing housing units, percent rural and percent suburban, fraction of commercial/industrial property, travel time to work, and the average MCAS score. As stated previously, many of the variables could have an impact on both supply and demand; this is a reduced form equation – we are not attempting to separate out the effects of supply from those of demand.

These controls explain 70% of the variation in the log of the average number of residential permits issued. Communities with larger populations issue more permits, as do younger communities. Higher density communities issue fewer permits, while rural communities issue more. Fewer permits are issued in high-income communities.

The regression also includes two variables meant to capture the ability of a community to afford new development. As discussed previously, new development imposes costs on local budgets that may exceed the additional property tax revenue. The two budget capacity variables reflect the constraints imposed by Proposition 2½. Under Proposition 2½, local property taxes can only grow by 2.5% annually, not including taxes on new growth and unused prior year capacity, without an electoral override. Even with such overrides, total property tax receipts can never exceed 2.5% of a locality's tax base or levy limit. The first of the controls, levy capacity, measures the amount that taxes can be raised without an override. The second, override

[54] The log of the number of permits is used because most towns issue few permits and a few towns issue many, i.e. the data is massed near zero with some outliers. The log of the number of permits has a more even distribution and the regression has a better fit. The results are similar but less precise if the number of permits is used instead of the log.

capacity, measures the amount by which a community could raise tax revenue if it resorted to an override, without violating the 2.5% levy limit.

The two budget capacity variables both have a positive impact on the number of permits a community issues. Towns with greater ability to raise revenue issue more permits. This supports the idea that towns may restrict development to prevent added fiscal burden; those towns that cannot afford development do not allow it.

Table 4: Housing Permit Regression Results[55]

Dependent Variable:
Log of Yearly Permits Issued, 1997-1999

Variable	Coef.	T-STAT
Log Population	0.36	1.89
Population Density	-0.20*	-8.82
Average Age	-0.06*	-3.58
Birthrate	51.8*	4.35
Log Income	-0.29	-1.04
Proportion Commercial/Industrial	-0.36	-0.81
Travel Time to Work	-0.01	-0.89
MCAS Score	0.00	0.40
Proportion Rural	0.63*	4.45
Proportion Suburban	-0.14	-0.80
Average Single-family Assessed Value	0.00	-0.02
Log Units	0.43	1.93
Log Override Capacity	0.33*	3.94
Log Excess Capacity	0.04*	2.42
Constant	-4.64	-1.71

The analysis was then repeated separately on single- and multifamily units and the number of single-family permits issued for units assessed at less than $200,000.[56] The statistical results are similar, with a few exceptions. Many of the characteristics that affect the total number of permits (population, density, age, birthrate, and income) appear to have little impact on the number of multifamily permits. The proportions of commercial and industrial property have a negative impact on single-family development and a positive impact on multifamily permits.

The budget capacity variables again explain a portion of the variation in the number of permits issued, although the results differ depending on the dependent variable. Once again, communities allow more development if they have the capacity to afford it. Both variables have

[55] Coefficients with a * are significant at the 5% level.

[56] 55% of communities in Massachusetts did not issue any multifamily permits during this time, and 15% did not issue any single-family permits for units valued at less than $200,000. The regressions were estimated using a tobit procedure to account for the censoring. The multifamily permit regressions included 341 observations (141 non-zero), and the low-value single-family permit regressions included 292 observations (245 non-zero).

a positive impact on single-family permits, but only the override capacity has a significant effect on lower value permits (excess levy capacity has a positive but not significant effect). For multifamily permits, neither variable has a significant impact.

Table 5: Housing Permit Regression Results, Single-Family, Multifamily, and Low-Value Permits[57]

	SF Permits		MF Permits		Permits < $200,000	
Variable	Coef.	T-Stat	Coef.	T-Stat	Coef.	T-Stat
Log Population	0.45*	2.60	1.78	1.79	1.01*	2.34
Population Density	-0.27*	-14.02	-0.03	-0.38	-0.15*	-2.70
Average Age	-0.07*	-4.35	0.08	1.10	-0.09*	-2.54
Birthrate	50.7*	4.80	13.4	0.25	12.6	0.53
Log Income	-0.10	-0.41	-1.29	-1.08	-2.28*	-4.13
Proportion Commercial/Industrial	-1.08*	-2.73	3.29	1.83	-4.49*	-4.66
Travel Time to Work	0.00	-0.50	-0.05	-1.11	-0.05*	-2.26
MCAS Score	0.00	0.13	0.02	0.51	-0.04*	-2.23
Proportion Rural	0.47*	3.74	0.20	0.37	0.91*	3.51
Proportion Suburban	-0.12	-0.77	-0.18	-0.29	-0.41	-1.20
Ave. Single-Family Assessed Value	0.00*	-2.98	0.01*	2.07	-0.01*	-6.12
Log Units	0.17	0.87	-0.30	-0.28	-0.75	-1.55
Log Override Capacity	0.47*	6.37	-0.33	-1.01	0.71*	3.98
Log Excess Capacity	0.03*	2.46	0.09	1.58	0.02	0.82
Affordability Mandate	0.38*	3.91	0.33	0.85	0.59*	2.75
Constant	-6.43*	-2.69	-3.66	-0.33	26.85*	4.85

The regression analysis above provides evidence that decisions about development depend at least in part on a town's ability to afford new residents. Towns that can afford development tend to issue more permits.

Looking into the limited data available on zoning corroborates this finding and suggests that the reason towns issue fewer permits is that they impose more restrictive zoning. The Executive Office for Environmental Affairs is currently conducting build-out analyses that project total new development that can occur within a community given existing zoning. Using this data allows a test of whether towns that face financial constraints are more likely to impose restrictive zoning. While it is difficult to quantify the severity of zoning ordinances, the analysis provides three potential measures. One is the proportion of land that is zoned for residential development, a second is the potential density of units allowed on developable land, and a third is the potential growth in the housing stock if all the allowed units were built. While each of these measures captures some aspect of a town's willingness to allow development, they all suffer from shortcomings. Perhaps the biggest problem is that zoning rules today are based not only on current political preferences, but also on past decisions that could stretch back decades. In addition, data used in this analysis were available to cover only 86 municipalities. Nevertheless, an analysis indicates that communities that have more budget capacity tend to have more lenient

[57] Coefficients with a * are significant at the 5% level.

zoning requirements. Specifically, a town's override capacity was significantly related to the proportion of land zoned for residential development and the potential growth in housing. Towns that are not constrained by Proposition 2½ seem to have more lenient zoning, which fits with the finding that they issue more permits.

Taken as a whole, the data suggest that the costs of new development influence communities' decisions about growth. Communities that face constraints on their ability to raise additional revenue issue fewer permits and appear to have more stringent zoning regulations. Tying some portion of local aid to the gap between property tax revenue and the costs generated by new development will remove the fiscal disincentive to allowing residential development and provide communities with the opportunity to relax limits on housing growth.

Special Cases

In addition to single family and multifamily housing, three types housing worthy of particular attention include student housing, single person housing, and public housing. Each of these is targeted at a narrow population, but they are important parts of the state's housing supply. Dedicated student housing reduces pressure on the supply in general. Single person housing and public housing serve low-income populations, who are least able to contend with scarcity and high prices.

Student Housing in Boston

Students make up a large portion of the population of Boston and can have a large impact on the housing market. The student population is worth studying separately because students, unlike other residents, have a clear choice between private housing and dormitories. Also, community policies influence the portion of students housed in dormitories instead of in private housing. A policy that diverts students to dormitories will reduce the overall demand for housing and relax the pressure on the housing market.

The 1990 Census provides data that can be used to analyze how students affect the housing market. In 1990, college students made up approximately 15% of the population of Boston. More than 70% of these students lived off-campus, most likely in rental housing. Students contribute to the demand for rental housing and, all else being equal, the increased demand should lead to higher rents.

The census data contains information on the residents and rents in Boston. In the 164 census tracts in the city, median rents averaged $620 and ranged from $152 to $1,001, while students living off campus made up between 1% and 66% of the total number of residents.[58] Regression analysis can estimate how the percentage of the population made up of college students housed off-campus will affect rents in that community. In addition to the number of students in the area, the regressions control for several neighborhood characteristics that could affect rents: the income and level of education of residents, median house value, the proportion of units that are owner-occupied, the proportion of units that are in large buildings (with more than 50 units), the number of bedrooms per unit, the density (people per unit), and the racial makeup of the census tract.

After controlling for these variables, areas with more students have higher rents. Specifically, a 10% increase in the fraction of the community made up of students who do not live in dorms leads to approximately a $75 increase in median rent. While the magnitude of this estimate is somewhat sensitive to which neighborhood controls are included, in all specifications the coefficient is positive and significant. Neighborhoods with higher proportions of students face higher rents.[59]

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[58] There were 169 tracts in Boston in the 1990 census, but 5 did not report any housing units. Resident counts include all residents not living in institutional or group quarters.

[59] The fraction of students was also a significant determinant of vacancy rates; areas with more students had lower vacancy rates.

Table 6: Median Rent Regression Results[60]

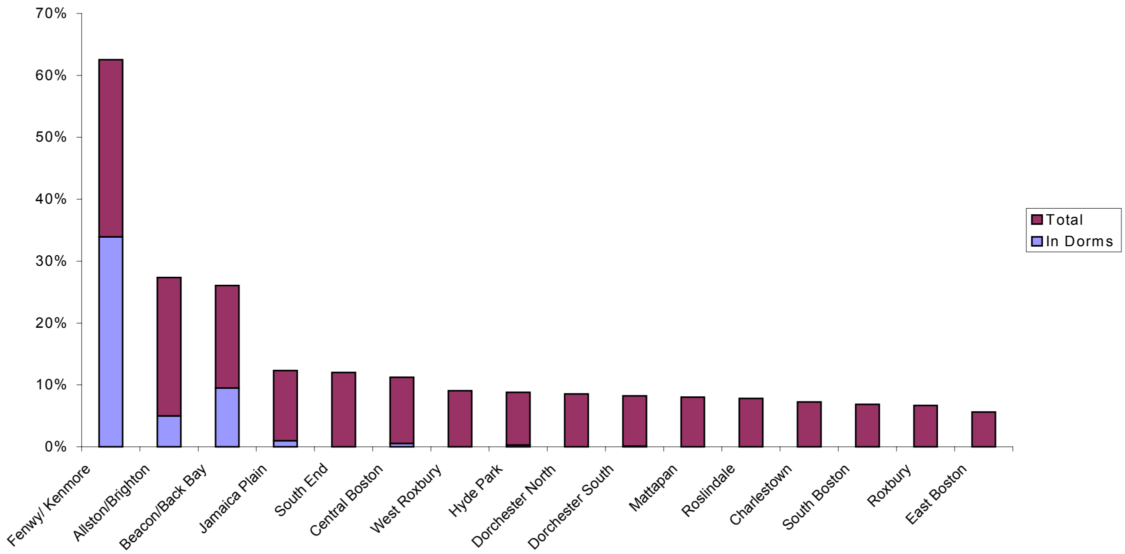
Dependent Variable: Median Rent

Variable	Coefficient	T-STAT
Median Income	0.020*	5.847
Median Income Squared	-2.4E-07*	-3.904
Median Home Value	0.0001	0.976
Proportion HH Owner Occupied	211*	2.422
Proportion of Adults with College Degree	395*	3.261
Proportion Units with 2 or 3 Bedrooms	510*	2.435
Proportion White	2.90	0.09
Population Density	120*	4.635
Proportion Large Buildings (50+ units)	179*	3.01
% Off-campus Students	7.41*	8.015
Constant	-396*	-4.462

The impact of students on the private housing market is compounded by the fact that students tend to be concentrated in very large numbers near existing campuses. As the graph below shows, the student share of a neighborhood's population ranges from as low as 6% in East Boston to as high as 26%-27% in Allston/Brighton and the Back Bay/Beacon Hill area. The Fenway/ Kenmore area is something of an extreme case with students comprising 63% of its residents, though most are housed in dormitories. Given the analysis above, these wide discrepancies in the concentration of students mean that in some neighborhoods students dramatically alter the rent levels. In Allston/ Brighton, for instance, the approximately 16,000 students in the private rental market (not in residence halls) could add more than $150 to the median cost of renting an apartment in that neighborhood.

[60] Coefficients with a * are significant at the 5% level.

Figure 16: Boston Higher Education Students as a % of Total Population by Neighborhood, 1990



Source: Boston Redevelopment Authority

Recent History

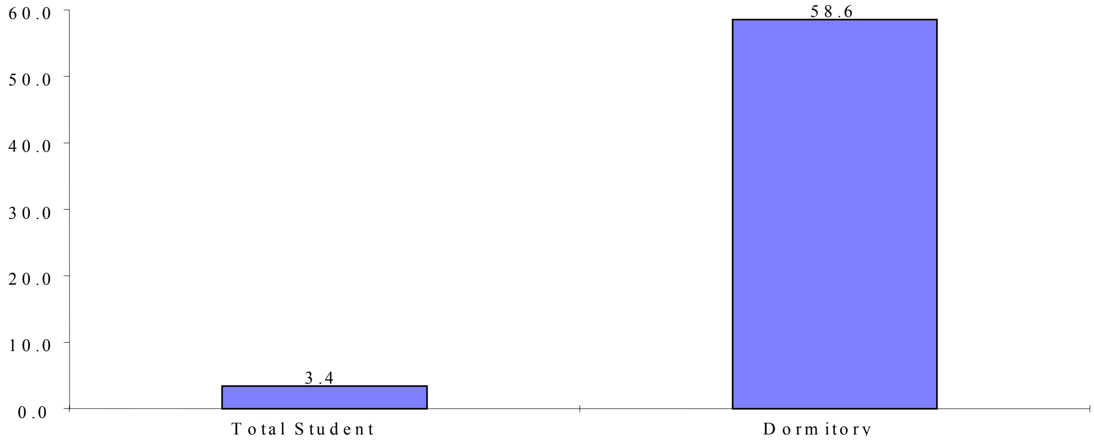
Several academic institutions have made significant progress building student housing in recent years. In the City of Boston, dormitory beds affiliated with its colleges and universities have increased by 58% from 17,968 in 1990 to 28,479 in 1998. Projects under construction or that are approved comprise a further 2,500 beds.[61]

This construction has occurred while total student enrollment at Boston colleges and universities increased by only 4,480. About, 44% of full-time undergraduates attending Boston colleges and universities now live in residence halls, with the number rapidly approaching 50%.

Student housing construction has occurred outside Boston, as well. The State College Building Authority is about to issue bonds to finance the building of a 300-bed residence hall for Bridgewater State College. In Cambridge, MIT is planning to build 350 new undergraduate beds on Vassar Street, 120 graduate beds on Albany Street and a further 600 to 700 beds for graduate students on the corner of Sidney and Pacific.

[61] Boston Redevelopment Authority, *Insight*, January 2000

Figure 17: Boston Enrollment and Student Housing Growth, 1990–1998



Source: Boston Redevelopment Authority

Impediments to Student Housing Construction

At first, it may seem like there is little need for public policy to encourage the construction of student housing. Many dormitories generate enough in housing fees to pay their operating and financing cost, so at least in these cases there do not seem to be significant financial impediments to construction. Colleges and universities recognize the value of student housing as an attraction for prospective students, so they should have an incentive to build the housing necessary for their student populations. And communities should appreciate that more student housing will decrease pressure on their private rental markets.

Unfortunately, other factors inhibit this confluence of interests. These factors include the lack of land availability, neighborhood opposition to institutional expansion, antiquated institutional guidelines for building student housing, a lack of desire on the part of institutions to be residential real estate managers, and limited ability to finance new construction. Because different combinations of factors apply to different institutions, institutional collaboration may offer an opportunity to overcome many of these hurdles.

Land and Neighborhood Opposition

Land availability appears to be a critical barrier to more student housing construction. Many of our universities are in older, denser communities like Boston, Cambridge, and Medford. In such areas, land is at a premium for any type of construction. However, land to build housing facilities for new students is particularly scarce. This is because some neighborhood groups often oppose university expansion, as can be seen with Northeastern University's recent Davenport Commons project and Harvard University's recent acquisition of property in the Allston area. In both cases, the institutions faced severe opposition to their expansion plans.

The opposition stems from several sources. Often communities fear new facilities mean more students, even if the university plans only to house existing students now living in the community. A community often sees additional students as sources of community disturbances and fears the erosion of its sense of identity. Where community/university relations are already strained, as is too often the case, community suspicion of new construction is exacerbated.

The case of Davenport Commons is instructive. Northeastern University sought to build student housing on Boston Redevelopment Authority (BRA)-owned land in Lower Roxbury to house 595 students. This project was part of a plan to reach a goal of housing 50% of its undergraduate population in student housing. Despite the fact that the initial plan included affordable units for the community as well as the promise of removing students from the private rental market, opposition coalesced from the outset. Opponents saw the new facility as an expansion of the university campus, which could ultimately lead to a displacement of a significant portion of the community. The use of BRA-owned land for the purpose further aggravated the situation, since neighborhood groups had long advocated for residential development of the property. Moreover, while nobody could be sure that students housed in the new facility would otherwise live in the Lower Roxbury community, the presence of the new student apartments was sure to concentrate a significant number of students in the area. Students housed in the private market may exert more pressure on rents, but they are also less visible than are those who live in a dormitory.

While the local opposition to this project was eventually mollified, it took three years to achieve an agreement with the community. Many schools may not have persevered so long. Other institutions, such as the Wentworth Institute of Technology, have had difficulty building even on land they own, due to community opposition.

Such opposition outside the City of Boston should have less of an impact than opposition within the city, due to the Dover amendment, which exempts colleges and universities from local zoning but does not apply in Boston. Nonetheless, schools across the Commonwealth, such as Salem State College, have faced local opposition to new dormitory construction, often resulting in the scrapping of projects altogether.

Land might be more plentiful to colleges and universities if they had better relationships with their communities. Clark University has taken significant steps to invest in its surrounding neighborhood through funding a community development corporation and various housing projects as well as providing community scholarships and mortgage subsidies to employees who live in the neighborhood. The result is that Clark University has little opposition to its expansion plans and has actually been given nearby abandoned properties taken over by the city.

While land is a critical barrier, it is not a universal one. Even in the Boston area, some institutions have land available. For instance, Lasell College in Newton had enough land to develop an assisted living development for seniors on its premises. Emmanuel College recently struck a deal with Merck Medco Corporation, allowing the pharmaceutical company to build a facility on their campus, the lease proceeds of which would help improve existing campus buildings. The Massachusetts College of Art has the capacity to build a 550-bed dormitory on a parcel of land now slated for a 300-bed facility.

Institutional Resistance

While almost all institutions recognize the advantage student housing provides in helping to attract students, some schools still resist becoming residential real estate managers. Others maintain guidelines governing the construction of dormitories that make further construction less feasible. Despite the rapid growth in dormitory construction in Boston in the last ten years, 43% of the institutions in the city provide no student housing at all.[62]

The reasons that institutions do not offer housing range from its cost to the fact that certain populations of students, such as part-time and graduate students, are not viewed as a potential market for student housing. In cases where a school has a high share of such students or a small student body overall, the anticipated costs of developing a housing program may seem daunting. For instance, typically a school would not only expect to need a real estate management office to manage its new facilities, but it would also need a new office for residence life to provide resident advisors, housing assignments, and extra-curricular activities. Public safety would need to be enhanced, as would potentially other services like computer labs, telecommunications, and food services. A school would also need to address a host of new issues like how to handle student-on-student crime.

Yet despite these drawbacks, demand for student housing is high even on traditionally commuter campuses. The University of Massachusetts at Boston held focus groups to determine the interest among its students and faculty in student housing. Even though there is currently no student housing and the school has emphasized its desire to be “commuter institution,” interest in student housing scored an average of 8.15 on a 10-point scale.[63] According to the focus group participants, housing would enhance a sense of community on campus, keep the campus active on weekends and evenings, increase the school’s applicant pool, and help retain students. It might also increase alumni identification with the campus and offer opportunities for conferences on campus. The report concluded that housing would be a positive benefit to the school even if it only served a small percentage of the student population.

For those institutions that have housing already, but have not engaged in growing their capacity in many years, one barrier may be strict guidelines that prevent the use of less costly building materials and methods. For instance, cinder block walls are often mandatory and some institutions require that toilet bowls be attached to walls rather than being allowed to rest on stands on the bathroom floor.

These restrictions have their genesis in ensuring the durability and ease of maintenance of the structures, particularly given the high wear and tear students can impose upon apartments. Nonetheless, as student housing evolves from the traditional dormitory into student apartments with kitchens and baths in the units, these restrictions lose some of their rationale. Moreover, with ever-changing technology and student tastes, the case for building dormitories to last into the next century loses much of its power. To provide the information technology infrastructure and amenities currently required in student apartments, many institutions must now engage in rehabilitation projects to century old buildings that are more costly than building from scratch.

Financing Capacity

While student housing usually provides sufficient fee income to pay for its operating and financing costs, this income stream is rarely leveraged to finance the facilities as stand alone projects. Rather, institutions usually pledge their whole balance sheet to guaranty the debt issued

[62] Boston Redevelopment Authority, *Insight*, January 2000

[63] University of Massachusetts Boston Student Housing Task Force, Initial Report, January 11, 2000, p. 5

for a project. The revenue bonds issued by the State College Building Authority in 1999 pledged all the revenues of the participating institutions including their state appropriations, not just the housing fees and revenues. The Massachusetts Health and Education Facilities Authority similarly reports that private colleges and universities have not financed their dormitories using "project-revenue bonds." This means smaller institutions may not have the financial wherewithal to fund housing projects. Larger institutions may want to preserve debt capacity for other projects such as teaching or athletic facilities.

Single Person Housing

At one time, low-income single individuals had access to more low-rent options, typically taking the form of single rooms with shared bath, kitchen, and living space, often referred to as single room occupancy units. Over the past several decades, the number of these options has declined. Between 1965 and 1985, Massachusetts experienced a 96% drop in single room occupancy units, the largest drop in the country.[64] The minimum housing standard that people find acceptable has risen over time and many now believe that studios and small one-bedroom apartments are more appropriate for many single individuals, but the availability of this type of housing is also limited and expensive for those with low levels of income. Throughout the Commonwealth, studios and one-bedroom apartments typically command rents that range from \$450 to \$900,[65] making even the relatively inexpensive examples of this type of housing effectively out of reach for individuals that earn less than \$1,500 per month, or \$18,000 annually.

Many of the Commonwealth's homeless shelter providers have suggested that a lack of low-cost rental housing for single adults has contributed to the growing number of homeless individuals. Although 48% of the Commonwealth's homeless individuals were employed in 1999, they earned income that averaged only \$1,018 per month for men and \$710 per month for women. Although the remaining 52% did not hold jobs in 1999, about 46% of the Commonwealth's homeless individuals reported unearned income, including income from such sources as social security, supplemental security, and supplemental security disability income.[66]

In recent years, the Commonwealth has been an active lender of funds for the development of housing for single persons. However, within the context of the Commonwealth's current housing shortage, there continues to be a deficiency of housing suitable for low-income single persons. To address this lack of low-cost housing options for single individuals, the Executive Office for Administration and Finance convened a working group to explore ways to support the development of such housing. The group included representatives from the Commonwealth's housing agencies, quasi-public housing agencies, and state government agencies within the

[64] The Brookings Institution, "*Setting Domestic Priorities*" (Washington, D.C., 1992)

[65] Derived from the Massachusetts Housing Partnership Fund Portfolio Management data; please note that the rents for studios and one-bedroom units vary widely across the Commonwealth; the range quoted above eliminates the extremes on both the low and high ends. Income required to afford rental units was based on the low end of the range of rental rates, and assumes that an individual could devote 30% of gross income toward housing costs.

[66] During 1999, homeless individuals reported a monthly average income of \$563 from social security, supplemental security, or supplemental security disability income. Center for Social Policy, John W. McCormack Institute of Public Affairs, University of Massachusetts, Boston, August 2000.

Executive Office of Health and Human Services.[67] Below is a summary of the group's findings and initiatives.

Background

Because there is no single type of housing suitable for all low-income single individuals, the working group coined the term "single person housing." For the purposes of this report, the term "single person housing" refers to housing intended for single persons of lower income who are homeless or at-risk of homelessness. These housing options include single rooms for rent with shared bath, kitchen, and living space as well as studio and small one-bedroom apartments. Various types of services may be made available both on- and off-site and can range from basic security and case management services to highly specialized services designed to meet the special needs of individuals with HIV/AIDS or persistent mental illness, for example.

It is important to note that many homeless and at-risk single persons facing a temporary crisis may only be in need of low-cost housing that is safe and secure, such as a room for rent in a safe and well run facility. Other at-risk single persons with specific physical and mental health issues may need a room or apartment of their own with supportive services available. The Working Group supports the development of all types of housing for persons with lower income.

The demand for publicly funded emergency shelter beds has increased over the last few years. To counteract this pressure, the Group's members agreed that policies that encourage development of housing options for homeless individuals and persons at risk of homelessness is an important step in the direction of homelessness prevention.

During the past 15 to 20 years, the Commonwealth has actively supported the development of different types of single person housing located in communities throughout the state. The agencies chiefly involved are the Massachusetts Department of Housing and Community Development (DHCD), the Massachusetts Housing Partnership Fund (MHP), the Massachusetts Department of Mental Health (DMH), and the Community Economic Development Assistance Corporation (CEDAC). During the Weld-Cellucci and Cellucci-Swift Administrations, the Department of Housing and Community Development has provided more than $16 million in state funds in support of single person housing development. During the same time period, the Massachusetts Housing Partnership Fund has provided almost $23 million in permanent debt for developers of such housing. In addition, the Department of Mental Health's Homeless Initiative uses $22.2 million in Commonwealth funding to leverage housing supply or subsidy resources primarily from the federal office of Housing and Urban Development. The Community Economic Development Assistance Corporation, meanwhile, has consistently provided both technical support and pre-development loans to non-profit developers, owners, and managers of single person housing.

Department of Housing and Community Development

In providing funds in support of single person housing development, the Department of Housing and Community Development has made a number of financing options available to developers. As described below, those financing options include the Housing Innovations Fund (HIF), the Massachusetts Rental Voucher Program, Section 8 Project-Based Rental Assistance, the Housing

[67] Members of the Working Group on Single Person Housing are listed in Appendix A.

Stabilization Fund, the Facilities Consolidation Fund, and the Individual Self-Sufficiency Initiative.

The Housing Innovations Fund (HIF)

During the past five years, the Housing Innovations Fund (HIF) administered by the Commonwealth's Department of Housing and Community Development (DHCD), has provided nearly $13 million in loans for the production or preservation of 1,159 units of single person housing. These units were located in 48 projects spread across approximately 23 different communities throughout the state. The HIF program, which is supported by Massachusetts bond funds, provides grants to non-profit developers of specialized housing.

DHCD prioritizes its HIF funding and targets housing for homeless individuals or families, disabled persons, elders, and low-income persons at imminent risk of homelessness. HIF has supported a wide range of single person housing, ranging from service-intensive projects for populations with special needs to close-to-market housing for single person working households.

The Massachusetts Rental Voucher Program (MRVP)

The Massachusetts Rental Voucher Program (MRVP), administered by the Department of Housing and Community Development (DHCD), provides project-based subsidies to specific housing developments under contracts between DHCD and private owners.[68] Owners agree to lease the units to income eligible households for a specified contract rent. Tenants pay a fixed percentage of their income toward that rent, and the Commonwealth covers the difference.[69]

MRVP project-based subsidies have been used extensively in the development of single person housing, supporting 32 projects in 15 communities. These projects have preserved or produced a total of 649 units, of which 502 are reserved for persons with MRVP tenant-based subsidies.[70] Some of these projects also received funding from the Housing Innovations Fund (HIF) and/or financing from the Massachusetts Housing Partnership Fund. Many of these units were developed in the 1980's and utilized a "moderate rehab"[71] approach in which MRVP project-based subsidies were used to guarantee a stream of income for five years to leverage financing from a variety of public and private sources.

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[68] "Project-based" subsidies are subsidies that are reserved for units in specific housing developments.

[69] The tenant's share of rent is 35% of net income if the contract rent includes heat and 30% of net income if the contract rent excludes heat.

[70] MRVP's tenant-based program provides a tenant with a voucher worth a fixed dollar amount, based on his/her income bracket. This subsidy can be used when renting any housing that meets the standards set by the Department of Housing and Community Development.

[71] The Moderate Rehab program was part of the former Chapter 707 rental assistance program, which provided a five-year rent guarantee in exchange for rehabilitating substandard rental property. This program did not provide a loan or grant, but did provide a five-year commitment of an income stream derived from the rental assistance program. The rental assistance is project-based, and the owner signed a five-year contract. When the Chapter 707 program was replaced with the MRVP beginning in 1992, the contracts for the Moderate Rehab program became one-year commitments with the option of being renewed on an annual basis. There have been no new commitments of Moderate Rehab funds since 1986.

Section 8 Project-based Rental Assistance

The Department of Housing and Community Development (DHCD) administers a 17,000 unit federally subsidized Section 8 voucher program. The vast majority of all authorized vouchers are utilized as tenant-based assistance.[72] However, DHCD administers vouchers at several Section 8 project-based single room occupancy (SRO) housing developments located throughout the Commonwealth. These project-based vouchers provide owners who lease to eligible households a monthly rental stream that represents the difference between 30% of the household's monthly-adjusted income and the "fair market rent" established by the U.S. Department of Housing and Urban Development for SRO apartments.

The Housing Stabilization Fund (HSF)

The Housing Stabilization Fund (HSF) provides money to support affordable rental and ownership housing throughout Massachusetts. DHCD makes HSF monies available to support the acquisition, demolition, rehabilitation, and construction of distressed and foreclosed properties as affordable housing. This program emphasizes strong community involvement in the design and implementation of efforts, which will respond to local priorities for neighborhood improvement. HSF is provided through the following three major initiatives: The Neighborhood Restoration Initiative, the Rehabilitation Initiative, and the Soft Second Loan Program.

Over the past five years, HSF has provided $49.5 million in funding for the rehabilitation and reuse of 2,457 units of housing in 72 projects located in 31 communities throughout the state. Of this, $4.0 million of funding was provided for the rehabilitation of nine distressed or abandoned properties containing 248 single room occupancy (SRO) units. HSF monies have been used as a single public source or in combination with other public funds including Low-Income Housing Tax Credits, Community Development Block Grant funds, and local HOME funds.

The Facilities Consolidation Fund (FCF)

The Facilities Consolidation Fund (FCF) addresses the needs of the institutionalized and underserved populations of Department of Mental Health and the Department of Mental Retardation as well as the mentally ill homeless. Funds are used for deferred mortgage loans to cover a maximum of 30% of the total development cost of housing projects, the majority of which are single person housing projects. It is a multi-agency program involving the Department of Housing and Community Development, the Executive Office of Health and Human Services, the Department of Mental Health, the Department of Mental Retardation, and the Division of Capital Asset Management and Maintenance. Since 1994, FCF has made about $14 million in commitments to 90 projects with a total of 580 units. This $14 million in FCF funding has leveraged over $58 million in additional resources.

A number of organizations, including the Department of Mental Health, believe that technical and/or design improvements to the program may increase the relatively limited interest among developers to gain access to available funds. For example, according to the Department of Mental Health and the Citizens' Housing and Planning Association: (1) the program imposes land use restrictions that are different from those of other financing programs; (2) the legislation has title reversion language that may serve as an impediment to attracting developers; and (3) the

[72] A "tenant-based" subsidy travels with a tenant. Tenants can use them to rent units that meet program housing quality standards and rent rules.

amount of funding allowed per project is a relatively small percentage of total development costs. Legislative design improvements in the program may make the Fund more useful and encourage more lenders to participate with the Department of Housing and Community Development in creating single person housing for persons with mental illness or mental retardation.

Individual Self-Sufficiency Initiative

In fiscal year 2000, Governor Paul Cellucci signed into law legislation that appropriated $1.25 million for the creation of the Individual Self-Sufficiency Initiative (ISSI). The ISSI is designed to assist homeless single person households who need a helping hand for up to twelve months to obtain permanent housing. For fiscal year 2001, the Governor requested, and the legislature appropriated, $2.5 million for the program. It is anticipated that this will provide assistance to at least 400 single person households throughout the Commonwealth through a network of regional non-profit housing agencies. This number of units is based on the maximum grant of $5,770 per household for fiscal year 2001, and includes both the resource and development models, described below.[73]

The ISSI provides up to $5,770 to a homeless individual whose income does not exceed 80% of the area-wide median and whose primary residence is a supervised public or private facility that provides temporary shelter. The program's objective is to move homeless individuals into single person housing units to promote self-sufficiency. Individuals who are residents of transitional housing may also apply. The ISSI is not a service-dependent program and each participant must be either employed or document that they are participating in, or have been accepted into, a vocational or employment training program that will enable them to achieve independence and self-sufficiency within twelve months. Service providers who have contracted with the regional non-profit housing agencies provide support services that program participants may require in order to successfully transition from a shelter environment to self-sufficiency.

The two components of the ISSI are:

1. The *Resource Model,* which helps to defray the costs for homeless individuals to obtain permanent housing by providing funds to pay for security deposits, first and last months' rent, moving expenses, or a monthly rent stipend. An individual who is in need of a rent stipend only, is eligible for up to $480 per month for a maximum of one year.

2. The *Development Model*, which may be used to provide a one-time financial gap filler for the development of new units of up to $5,770 per unit. As a requirement, these units must be made available to ISSI eligible applicants for a minimum of five years at rents affordable to them. A non-profit agency or a private owner may develop units using this model.

The ISSI is a new approach to addressing the issue of homelessness and provides an alternative program for persons who are ready to make the move from a shelter environment to a more viable housing option.

[73] This amount excludes the administrative fees of the regional non-profit housing agencies.

The Department of Mental Health

Through its Homeless Initiative, the Department of Mental Health (DMH) uses Commonwealth funding to leverage housing supply or subsidy resources primarily from the federal Department of Housing and Urban Development. DMH is almost never a grantee of these resources, but collaborates with the Department of Housing and Community Development and numerous local housing and community development agencies across the Commonwealth to gain access to housing resources for its clients. With such collaboration, DMH is able to leverage $22.2 million in Commonwealth resources to secure over $71 million in federal funds.

The Department's Homeless Initiative was established in 1992 with support from the Administration, the legislature, and homeless advocates. What began as a $1 million program with state appropriated funds in fiscal year 1992, grew to $21.2 million in annualized state funding in fiscal year 2000. A $1 million expansion is planned for fiscal year 2001. The primary goal of the Initiative has been to address the cyclical nature of homelessness by creating transitional and affordable permanent housing with a full range of support services designed to help individuals recover from their mental illness to the fullest extent possible and live successfully in the community. It has provided a range of community-based services, such as emergency services, counseling, referral, and case management to a total of 6,633 homeless individuals. Support services include counseling, case management, education and training, clinical care, and first aid.

Local community housing organizations sponsor the state or federal grant applications for permanent and transitional housing dollars. Federal applications often require that state dollars be identified to fund support services and/or to match the federal grant. DMH Homeless Initiative funding provides for residential and other support services in conjunction with the housing resources. Through this program, 961 new housing units have been leveraged or accessed from state and federal housing programs. Through the utilization of these units and others, DMH has been able to place 1,916 homeless individuals into new or existing housing with residential support and/or community-based services.[74]

Community Economic Development Assistance Corporation (CEDAC)

Over the past 20 years, the Community Economic Development Assistance Corporation (CEDAC) has consistently provided both technical support and pre-development loans to non-profit developers, owners, and managers of single person housing. They have also underwritten Housing Innovations Fund (HIF) and Facilities Consolidation Fund (FCF) loans, on behalf of the Massachusetts Department of Housing and Community Development, to finance many of these developments. This underwriting has required a thoughtful review, not only of the financial and business aspects of the development, but of any supportive services that may be required by the residents, as well. The result has been that since 1980, over 2,500 housing units have been created or preserved for low- to moderate-income single adults.

The Massachusetts Housing Partnership Fund

The Massachusetts Housing Partnership Fund (MHP) has been actively involved in the financing of single person housing since it began financing affordable housing in 1992. At present, MHP's

[74] This number includes all clients who "moved in" regardless of length of stay. It is exclusive of client relocations and, as such, is an unduplicated count of placements.

single person housing portfolio consists of 33 loans covering 1,304 units in 27 communities throughout the state. Of these units, MHP requires the owners to keep 919 units affordable to one-person households with income below 50%, 60%, or 80% of the community's median income (MHP requires its borrowers to meet affordability in one of three ways: 20% of the units must be for households at or below 50% of median income, or 40% at or below 60%, or 50% at or below 80%). These figures are likely to understate the actual affordability being accomplished through their financing, as MHP believes that the majority of the residents in these buildings are of low- or moderate-income.[75]

MHP's single room occupancy properties have affordable units that can be rented by one-person households with incomes no higher than 50% to 80% of the community's median income, depending upon the property. This means that MHP's affordable single room occupancy units in Boston must be rented to one-person households with annual incomes no higher than $23,000 to $35,000. For those individuals in Boston, the restricted rents range between $430 and $650 per month.[76] In Springfield, where median incomes are lower, MHP's single room occupancy properties have affordable units that can be rented by one-person households earning no more than $17,000 to $27,000 per year. For those individuals in Springfield, the restricted monthly rents are in the $315 to $500 range.

Rather than financing new construction, MHP's loans for single person housing have involved the acquisition and rehabilitation of operating properties, or substantially vacant buildings. The capital needs of these properties have tended to exceed what can be conventionally financed, which is why most of MHP's loans are accompanied by "soft" financing -- outright grants, or loans not requiring current loan payments, which typically are provided by other government sources. Several of these properties, however, have received subsidies from MHP's own Permanent PLUS program, a demonstration program which has provided 0% interest, deferred-payment second mortgages to help meet a project's capital needs without imposing additional debt service burdens.

Key Issues

As described below, the working group determined that efforts to encourage single person housing should consider:

- the need for gap financing;
- the cost of services;
- inflation;
- management challenges; and
- the needs of the community.

[75] According to the Massachusetts Housing Partnership Fund, the key growth area in households at risk of homelessness is in the 30%-to-50% of median-income range.

[76] "Restricted rents" are rents that are limited as a condition of financing by a public or quasi-public entity.

The Need for Gap Financing

For most single person housing projects, there is a substantial gap between total development costs and the maximum amount of debt that investors are likely to support. When the working group examined the financial characteristics of single person housing for projects that received financing from both the Housing Innovations Fund (HIF) and the Massachusetts Housing Partnership Fund (MHP), the average supportable debt was about $16,000 per unit. This compares to an average per unit development cost of $60,000 to $75,000. The result is a significant need for gap financing that can run between $44,000 and $59,000 per unit.

A similar analysis conducted by the Massachusetts Housing Finance Agency examined the financing structure for a hypothetical single person housing unit costing $60,000 (the low end of the development cost range) targeted for individuals at risk of homelessness. The analysis assumed that the unit would generate revenue of about $100 per week from unsubsidized rent collections, totaling $4,784 annually.[77] A rent level of $100 per week, or $433 per month would be affordable to a single person earning $1,444 per month ($17, 328 per year) who spends 30% of his/her income on housing costs. However, it is important to note that individuals collecting income from social security, supplemental security, or supplemental security disability income often have significantly less than $100 per week available for rent.[78]

Assuming $4,784 of revenue per year and annual operating expenses of $3,700 (assuming no expenses related to services), and a debt service coverage ratio of 1.15, only $943 of net operating income per year would be available for debt service.[79] With only $943 available for debt service annually, the maximum amount of mortgage that lenders would support would likely be approximately $10,000.[80] A total development cost of $60,000 would therefore require that the developer find an additional $50,000 of equity, or gap financing per unit.

Single person housing developments, absent rental subsidies, support very little amortizing debt, and therefore require substantial equity or gap financing to cover total development costs. In the single room occupancy housing projects examined, most developers were required to pursue capital resources from multiple public or quasi-public sources. The only exceptions were a few non-profit sponsors that were able to acquire properties under very favorable conditions. The need for developers to piece together financing and funding from numerous municipal, state, federal, and private resources presents a particularly time-consuming and cumbersome challenge for sponsors interested in developing housing for low- and moderate-income single individuals.

Cost of Services

For properties that target service-dependent populations, it is critical for subsidy providers and debt underwriters to examine potential funding needs related to service delivery. A traditional real estate financing approach, one that recognizes only the real estate operating costs as if the property were a conventional apartment property, would require that the owner continuously

77 Revenue estimate assumes $100 per week x 52 weeks less vacancy rate factor of 8%.

78 During 1999, homeless individuals reported a monthly weekly income of $130 from social security, supplemental security, or supplemental security disability income. Center for Social Policy, John W. McCormack Institute of Public Affairs, University of Massachusetts (Boston: August 2000)

79 Calculation of amount available for debt service: ($4,784 - $3700) / 1.15 = $943

80 Assumes an interest rate of 8.3% and a term of 30 years.

fund-raise for the provision of services that are critical for the residents and the financial stability of the property. This does not mean, however, that service funding should be used to cover non-service related operating expenses. Instead, potential service funding needs should be examined. The absence of long-term service funding commitments may act as an impediment to securing financing closure, since continuity of services can affect an owner's ability to maintain high occupancy and rent collections.

Inflation

Real estate and service-related expenses are subject to inflationary pressures. Therefore, project-based or operating subsidies must allow owners to increase revenues to cover these increases in costs. Some subsidy programs applied to single person housing properties, especially those housing populations with little or no capacity to pay rent, have lacked means of allowing the programmatic rent revenues to increase to keep up with the inflation that applies to both the real estate and service costs of operating these properties. This puts these properties into potential operation deficits soon after they begin operations.

Management Challenges

Single person housing represents a specialized type of rental property. There are a limited number of developers who can develop and manage this type of property well, which contributes to the current shortage of this type of housing. Compared with the demands of conventional apartment properties, single person housing requires an experienced owner and hands-on property management. In some developments, tenants will move in and out more frequently, put more wear and tear on the buildings, and pay rent weekly rather than monthly. In addition, due to typically small project size, single person housing is more sensitive to loss of rental income due to vacancies, non-payment of rent, and tenant turnover. All members of the working group agreed that a smoothly functioning single person housing property must have a highly active management program, regardless of its target population. For buildings of ten or more units, this requires, when feasible, that a resident manager be present who knows the residents and is aware of their daily needs and activities. In some cases, the resident managers act as both a property manager and a service coordinator (case manager); however, some projects need one of each type of manager. For smaller properties, while resident management may not be economically feasible, the property owner must maintain a constantly visible profile by assigning someone dedicated to the property to perform this function.

The Needs of the Community

All members of the working group agreed that there are three primary ways that the Commonwealth makes the effective siting and ongoing community acceptance of single person housing projects possible: 1) by encouraging the development of well-managed properties; 2) by ensuring that new construction or building rehabilitation projects meet high quality standards; and 3) by requiring that projects go through a community review process.

First, by encouraging the development of well-managed properties, the Commonwealth plays an important role in ensuring that development projects will meet the needs of their communities. For example, when a developer of single person housing applies for funding from the Commonwealth's housing or quasi-public agencies, it must demonstrate a proven and successful track record in managing this type of property and extensive experience in providing housing for the property's targeted population. If service-needy populations are targeted, the developer must demonstrate that there will be close daily cooperation between those responsible for services and those responsible for property management. Similarly, the developer must be able to describe, in general, the service package that would be appropriate for the targeted population. When the financing is close to closing, the developer must present a detailed service plan with the appropriate commitments from service agencies.

Effective service plans typically include methods for screening prospective tenants, for determining each new tenant's medical or job referral needs and for implementing those needs, as well as a plan for determining if and when the tenant either needs housing with supportive services or is ready for a more autonomous residence. Developers must demonstrate that when situations arise with service-needy tenants, in particular, managers have a track record of taking action promptly, meeting tenants' needs, and addressing any appropriate concerns of members of the surrounding community.

Secondly, by ensuring that new construction or building rehabilitation projects meet high quality standards; properties are likely to become important neighborhood assets. In fact, there are numerous examples of state-supported renovations of buildings for single person housing throughout the Commonwealth that have led to new private investment in nearby properties.

Finally, it is important that the Commonwealth continue to take seriously the concerns of communities when siting publicly funded single person housing projects, involving the community in discussions about the projects, and addressing community concerns.

Public Housing

In this time of rising rents and demands on the homeless shelter system, the Commonwealth's 50,000 units of state-aided public housing are an increasingly important resource. (There are an additional 34,000 units of federally-aided public housing.) State-aided public housing is diverse in the people it serves—more than 32,000 elderly households, 15,000 families and 3000 special needs units for mentally ill and mentally retarded individuals; in its location—235 communities across the state; and in its design—from single-family homes to townhouses to high-rise senior housing developments. Yet all 50,000 units share a common thread—providing a stable home that is affordable to anyone, no matter how low their income.

The housing was made possible through a massive commitment of public resources over the past fifty years—over $2 billion for its development and modernization. While other programs address some of the low-income housing needs of the Commonwealth, public housing remains the largest state housing program by a significant margin in terms of households served. This resource is even more valuable in an environment where some units may be taken out of the affordable market as a result of the expiration of their subsidized mortgages or Section 8 contracts over the next ten years. While not without its troubles, state-aided public housing has provided countless senior citizens, individuals with disabilities, and families with homes they could afford. To replace this critical component of the Massachusetts housing supply today would cost (conservatively) more than $7 billion, if it were even possible.

State-aided public housing has also been the most economical program providing housing for the poorest of the poor, as the following chart shows.

Cost/Unit For DHCD Housing Programs Serving Families With Incomes Below 30% of Area Median Income				
Housing Program	**Total Cost**	**Total Units**	**Monthly Cost Per Unit**	**Annual Cost Per Unit**
Public housing - family & elderly FY 2000 (excludes special needs units)	$72,937,484	46,964	$129	$1,553
MRVP	$30,464,172	6,831	$372	$4,460
AHVP	$3,155,076	702	$375	$4,494
Section 8 voucher/certificate	$106,844,340	14,504	$614	$7,367

The problems of many federal public housing developments across the country—primarily dense, high-rise family developments—have shaped the public's conception of public housing in general. However, the state public housing portfolio, while sharing some of these problems, has some fundamental differences. These problems, and differences, include:

- a concentration of poverty with too few residents gainfully employed. Until the 1960s, the median income of public housing residents was at approximately the 33rd percentile of household income nationwide; in recent times it fell below the 10th. But the strong economy and regulatory changes like welfare reform have lifted the typical median income of state public housing families to an estimated 15 to 20% of area median income—still low, but rising.

- isolation from surrounding communities. Large public housing developments can be insular. However, the typical state family public housing development is limited in size, with no high-rise developments, and only 46 developments housing more than 100 families.

- a lack of incentives for managers to maintain high "market" standards. With long waiting lists of housing-distressed people, housing managers have limited inducements to maintain a high quality project. Few family public housing developments would be able to market their units to unsubsidized residents.

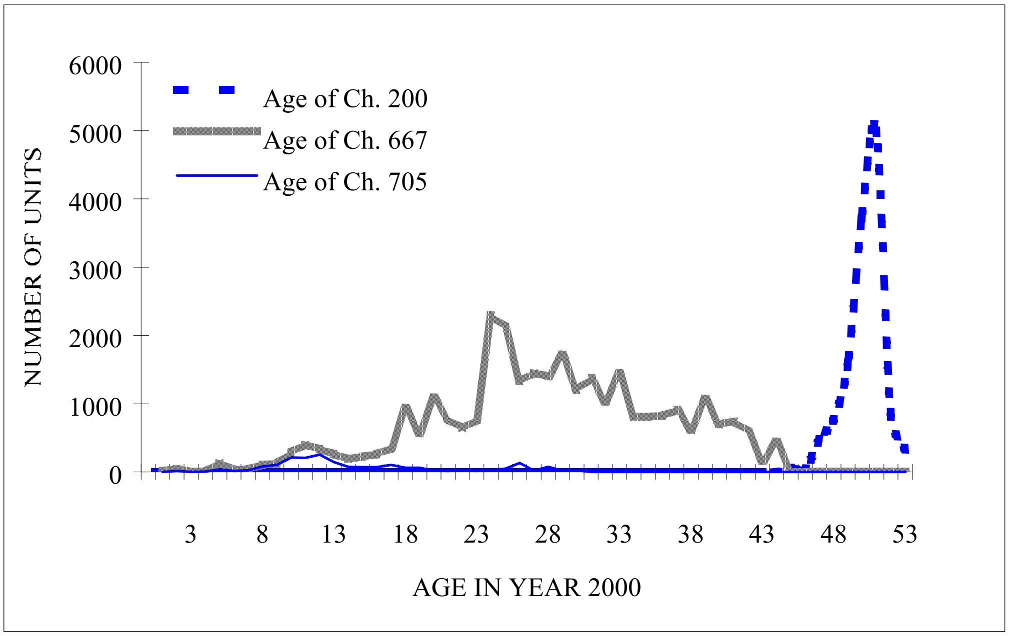
Since these issues afflict public housing nationwide, the viability of public housing as currently structured is being challenged. Neither the Commonwealth nor the U.S. government is undertaking significant new development of public housing. (The state is finishing a limited number of existing development commitments.) Instead, state and federal efforts to address housing needs now focus on using grants or loans, low-income housing tax credits, and tax-exempt financing to encourage the private development of affordable housing. The U.S. Department of Housing and Urban Development (HUD) is currently more than half of its way through a plan to demolish 100,000 distressed federal public housing units.

Capital Needs

Among the Commonwealth's public housing portfolio, few units today require such drastic action. Yet preservation of the state's public housing assets for the future will require careful planning and investment.

In the early days of the state's public housing program when the housing stock was relatively new, the need for capital improvements was limited. It was not until 1985 that the average age of all state elderly and family units exceeded twenty years, the time when many building components begin to reach the end of their expected useful lives. Today, that average age is 34 years and climbing. Roofs, plumbing and heating systems, and wiring need replacement, and kitchens and baths are worn out from decades of use.

Figure 18: Massachusetts Public Housing: Age in Year 2000, by Program



As Figure 18 indicates, the Chapter 200 family housing portfolio long ago reached this point; the typical unit is about fifty years old. Now, the much larger Chapter 667 elderly housing portfolio is entering old age, bringing its own of demand for capital improvements. This "graying" of the public housing stock poses a significant challenge to our ability to meet the basic physical needs of our 50,000 units of housing.

The Commonwealth has over the last decade shifted its emphasis from developing new public housing to modernizing and preserving the existing stock. It has devoted considerable resources to do so. But the sheer size of the portfolio—by far the largest state-aided public housing program in the country on a proportional basis—makes it difficult to keep pace with capital needs. The state Department of Housing and Community Development can provide funds only for the most pressing capital needs. This is, in and of itself, problematic and could also create a perverse incentive for housing managers to let developments deteriorate so they can access state funds.

Legislative Limitations

In addition to capital improvement needs, the public housing portfolio also finds itself hamstrung by a statutory framework that limits the ability of local housing authorities to respond to local needs or changes in the local housing market. These limitations include:

- a legal structure for the design and bidding of public construction projects that was developed to guard against corruption on large-scale projects, but which significantly increases costs and slows down schedules on even relatively small and simple capital improvement projects.

- statutes that prohibit the transfer of overhoused “empty nesters” in large family units to one-bedroom elderly units, a resource-efficient practice that could serve many needy families now languishing on waiting lists without the expenditure of any funds for construction.

- statutes that prohibit the admission of applicants under the age of 60 without a qualifying disability to elderly housing, even when there is no waiting list and units may be vacant.

- a mandated rent structure that introduces inequity among tenants and deprives housing *authorities* of needed rent revenue by requiring that tenants paying for all their utilities, including heat, pay the same portion of their incomes for rent as those paying only for their own electricity.

Affordable Housing in Massachusetts

Federal Affordable Housing Programs

The federal government over much of the twentieth century created and expanded a series of programs intended to provide housing for low-income households.

Public Housing. Beginning in the Great Depression, the federal government authorized the Reconstruction Finance Corporation to lend money for the construction of housing for low-income families. In 1933, the National Industrial Recovery Act authorized the creation of public housing authorities and federal funding for slum clearance and the construction of low-income housing. In 1937, the Public Housing Administration was formed to build low-income housing through long-term, low-interest federal loans and annual subsidies to cover debt service.

Privately Owned Assisted Housing. During and after World War II, several initiatives were launched to provide housing for defense workers or to help returning veterans buy houses. The Housing Act of 1949 funded 810,000 units of public housing over the next six years and created the rural housing program in the Farmers Home Administration. In the 1950s, attention turned to creating low-rent housing for the elderly, culminating in the creation of the still-operating Section 202 program in the Housing Act of 1959. The 1960s saw the creation of the U.S. Department of Housing and Urban Development as a cabinet-level agency, the outlawing of housing discrimination, and the expansion of federally sponsored programs to provide mortgages and mortgage insurance to promote homeownership. In 1968, the Housing and Urban Development Act created the Section 236 program that provided interest subsidies for the construction of low-income rental housing.

Section 8. The mechanism for funding affordable housing then changed to stress rent subsidies, either to projects or directly to tenants. The Housing and Community Development Act of 1974 established the Section 8 leased housing program that is today the largest affordable housing program in the country. Amendments to that law in 1981 targeted federal Section 8 and public housing for the most needy households and required participants to pay 30% of their incomes for rent. In 1983, Section 8 was further changed to eliminate new construction and to create the Section 8 voucher program that changed the way the tenant's and government's contribution to an apartment's rent were calculated.

Tax Credits and Tax-exempt Bonds. In the 1980s, the use of bonds exempt from federal taxes and then, under the Tax Reform Act of 1986, the use of federal low-income housing tax credits (normally allocated by states) became the dominant source of government funding for affordable housing projects. States and local governments assumed an increased role in federal housing programs with the creation of the HOME program, a block grant program for housing, by the Affordable Housing Act of 1990. HOME replaced the rental rehabilitation and Housing Development Action Grant programs, and the act also further limited Section 8 by ending the moderate rehabilitation program (except for a special program to assist with homelessness). The federal government also took steps toward allowing the disposition of public housing, first by transfer to resident management corporations and later, under the HOPE VI program, by outright demolition.

State Affordable Housing Programs

Almost uniquely among states, the Commonwealth has significantly augmented the housing produced by a series of federal programs with substantial assisted housing programs of its own.

Public Housing. These state housing programs stretch back to the years immediately following World War II, when Chapter 200 of the Acts of 1948 authorized the State Housing Board to undertake the construction of safe, decent housing for veterans returning from World War II. Over the next five years, 136 Chapter 200 developments with 15,462 units of veterans' housing were built, at a total cost of $187,406,000. The projects were financed by forty-year bonds sold by local housing authorities. The bonds were guaranteed by the full faith and credit of the Commonwealth, and contracts for financial assistance (CFAs) were executed with the authorities that committed the Commonwealth to making annual payments of the interest and principal due on the bonds. Operating costs were at that time covered by rental payments, which were based on cost of operating the development rather than on a percentage of family income, and there was no provision for a state operating subsidy. After passage of the "Baby Brooke" amendment to Chapter 121B of the General Laws in 1971 limiting rents to 25% (later changed to 30%) of tenant income, the Commonwealth began to subsidize the operating deficits of housing authorities. It continues to do so today. The State Housing Board became the Department of Community Affairs, which was made part of the Executive Office of Communities and Development, which was succeeded by the Department of Housing and Community Development, but more than 13,000 of these Chapter 200 units remain and continue to house Massachusetts residents.

Later, the Chapter 200 portfolio was joined by the housing units for the elderly authorized under Chapter 667 of the Acts of 1954. Between 1954 and 1995, 582 Chapter 667 developments containing more than 32,000 units were built in 233 cities and towns. In the 1970s, non-elderly disabled families and individuals were made eligible to reside in Chapter 667 housing.

Chapter 705 of the Acts of 1966 provided for the construction or acquisition of a new, scattered site portfolio of family public housing that now comprises more than 2000 units. Of similar size is the portfolio of special needs housing developments built under Chapter 689 of the Acts of 1974. Together, these programs provided more than 50,000 units of state-aided public housing, a portfolio significantly larger than the 35,000 units of federally-aided public housing in the state. Massachusetts is one of the few states that ever built state-aided public housing, has the largest such portfolio on a per capita basis in the country, and has the second largest program in absolute terms behind New York -- a state three times Massachusetts' size whose portfolio is only 20% larger.

Rental Assistance and Project-based Subsidy of Privately Owned Assisted Housing. Massachusetts has gone well beyond public housing to provide affordable homes for Massachusetts residents. Chapter 707 of the Acts of 1966 created a state program to provide project-based assistance to privately owned, low-rent housing projects and rental subsidies. Chapter 707 ultimately grew to be the largest and most expensive program of its kind in the nation. In fiscal year 1993, the 707 program was replaced by the Massachusetts Rental Voucher Program (MRVP).

Interest Subsidy. Chapter 708 of the Acts of 1966 created the Massachusetts Housing Finance Agency (MHFA). Since its creation, MHFA has provided financing of $3.5 billion for more than

600 multifamily developments containing 74,000 rental units. In addition, MHFA has provided a total of $2.8 billion in mortgage financing for the acquisition and rehabilitation of one- to four-unit properties serving more than 43,000 low- and moderate-income households. MHFA operates by borrowing funds, usually at tax-exempt interest rates, and then lending the proceeds of these funding bonds for below-market-rate single-family mortgages and for the development or rehabilitation of low- and moderate-income rental properties. MHFA supports its operations from fees and the spread between its borrowing and lending rates. As explained below, MHFA projects in specific state programs receive state subsidy beyond the federal subsidy inherent in its tax-exempt borrowing.

In 1970, Massachusetts created a state analog to the federal Section 236 interest-subsidy program by passing Section 10 of Chapter 855 of 1970, which amended MHFA's enabling act to add Section 13A. Ultimately 59 developments with 7,006 units were built under the 13A program, accounting for $214 million in MHFA financing (and another 5 developments – representing 1,266 units and $41 million in financing -- which were developed with a combination of Section 236 and 13A assistance). The Commonwealth continues to subsidize these loans to write the interest paid by the developments attributable to low-income units down to a rate of one percent.

State Aid for Rental Production. The 1980s were the era of a real estate boom in Massachusetts that in most respects dwarfs what has been happening over the last several years. Prices went up faster, and production rose. Nonetheless, it was determined that an insufficient amount of rental housing was being produced and that production would remain too low without more government assistance. As a result, the State Housing Assistance for Rental Production (SHARP) and Rental Housing Development Action Loan (RDAL) programs were implemented. The SHARP program built 9,383 units in 82 developments, and an additional 643 units in five developments representing $46 million in MHFA financing were developed using the RDAL program. RDAL was also used to provide additional subsidy for 517 low-income units in 14 of the 82 SHARP developments mentioned above. In addition, the TELLER program allowed local housing authorities to issue tax-exempt debt for the private development of low- and moderate-income housing developments.

In the SHARP program, MHFA made loans for the development of properties based on the premise that the state would pay a subsidy that was scheduled to decline over fifteen years as net operating income increased. The subsidy payments are given as loans that are to begin to be repaid at a later date. The Commonwealth continues to pay SHARP and RDAL subsidies.

However, many SHARP developments were underwritten using grossly over-optimistic assumptions for growth in net operating income. As a result, developments would be unable to make their loan payments according to the original declining subsidy schedule. In addition, many developments were unable to meet debt obligations even with state subsidy support. These developments were given additional "operating deficit loans" by MHFA in the early 1990s so that they would be able to make their first mortgage payments. Although the SHARP portfolio added over 9,000 units of high-quality, mixed-income housing to the affordable inventory, these developments were not financially sustainable over the mortgage term. MHFA commissioned a study in 1997 that found a $500 million deficit in the program and proposed innovative solutions within the real estate portfolio itself to address this problem. MHFA has made significant progress in implementing these strategies and has negotiated financial solutions for more than half of the portfolio.

Massachusetts Housing Partnership. Beyond these programs, the Commonwealth has set up a unique private financing structure to provide additional resources for affordable housing development and preservation. Established by state law in 1985, the Massachusetts Housing Partnership Fund has obtained more than $440 million in credit at below-market rates as a condition of state approval for certain bank acquisitions. These loan funds are combined with other funding, including bank grants, to provide long-term financing for affordable rental housing and have supported the rehabilitation or construction of nearly 8,000 apartments since 1992. The Commonwealth has contributed $4.5 million since 1998 that serves as a capital base for MHP's borrowed funds; every dollar appropriated by the Commonwealth has leveraged more than twenty-five dollars in below-market financing.

Other Ongoing State Funding for Affordable Housing. The Commonwealth also funds ongoing programs that use state capital funds borrowed by the state treasury to provide grants and loans for the development and rehabilitation of affordable housing. These include the Housing Stabilization Fund, the Capital Improvement and Preservation Fund, the Housing Innovations Fund, and the Facilities Consolidation Fund. In addition, a number of annual appropriations assist with affordable housing, including funds to make low-interest loans for first-time homebuyers and for the remediation of lead-based paint hazards and the installation or upgrade on septic systems required by Title 5.

New Funding Initiatives. Beyond these well-established programs, the Commonwealth has recently adopted and provided $200 million to be committed over the next five years by two new affordable housing programs. First, the State Low Income Housing Tax Credit Program, based on the federal program whose name it shares, will allow the Department of Housing and Community Development (DHCD) to allocate a five-year stream of state income tax credits to a qualified affordable housing project. The project sponsor then uses or, more often, sells the tax credits to investors. Second, the state Affordable Housing Trust Fund will be able to make loans or grants to fund a wide variety of affordable housing development, preservation, and homeownership projects. The program will be administered by the Massachusetts Housing Finance Agency with input from an advisory committee under guidelines issued by DHCD.

The state is also active in the ongoing effort to expand the funds provided by the federal Low Income Housing Tax Credit program and by tax-exempt private activity bonds that can be used to finance affordable housing projects. The availability of funds provided by both of these programs is constrained by a per-capita limit imposed in 1986. Federal law authorizes states to issue annually tax credit allocations of $1.25 per capita and tax-exempt private activity bonds of $50 per capita. This means that Massachusetts can issue approximately $7.5 million in federal tax credit allocations per year, which result in nearly $60 million in equity from private investors. The Commonwealth can also authorize nearly $309 million of tax-exempt private activity bonds per year. For calendar year 2000, the Commonwealth has assigned $123.5 million, or 40% of the total private-activity ceiling, to affordable housing use, including rental housing production and preservation and below-market interest rate mortgages for first-time homebuyers.

The per capita limits on low-income housing tax credits and tax-exempt private activity bonds were fixed by federal law in 1986. Since then, they have lost more than one third of their purchasing power due to inflation. Federal legislation has been filed to increase the per capita limits on both of these programs in each of the last several congressional sessions. These proposals have enjoyed widespread support but have failed to become law because the larger bills of which they were a part met with opposition. Bills are currently pending in Congress to raise the per capita limits on both programs, and some proposals would also index them to inflation in the future. The pending bills would go a long way toward regaining the original value of both instruments by increasing low-income housing tax credits from $1.25 to $1.75 per capita and the state ceilings on tax-exempt private activity bonds from $50 to $75 per capita. To regain their 1986 purchasing power, low-income housing tax credits would have to be increased to $1.94 per capita, and private activity bond caps would need to equal $77.70 per capita.

The Weld-Cellucci and Cellucci-Swift Administrations have been strongly in favor of increasing the per capita limits on low-income housing tax credits and tax-exempt private activity bonds. The Governor and Lieutenant Governor have advocated for immediate increases to the proposed amounts, rather than the three-year phase-ins called for in some proposals. If Congress and the president were to enact the proposed per capita limits as proposed, Massachusetts would be able to issue an additional $3 million in federal low-income housing tax credits, which could be expected to raise well over $20 million of additional equity investments in affordable housing developments per year. In addition, the proposed increases in per capita limits would allow more than $150 million of additional tax-exempt private activity bonds per year in Massachusetts. The Commonwealth could then commit additional resources to below-market rate mortgages for first-time homebuyers and for affordable housing development and preservation.

Current Affordable Housing Programs in Massachusetts

The result of a half-century of affordable housing programs is that a significant portion of the Massachusetts rental housing market is subsidized in one way or another. Nearly one quarter of Massachusetts rental tenancies either exist in units developed, rehabilitated, or operated using public subsidies or are occupied by tenants who have rental subsidies. Such a high number of Massachusetts tenancies are subsidized because of both a disproportionate share of federal housing assistance and the addition of tenancies subsidized by sizable state programs.

The role Massachusetts has taken in addressing the housing needs of their citizens is even more distinctive when put in a national context. When it comes to supporting affordable housing, Massachusetts is literally in a league of its own. Many other states rely exclusively on the federal government for public housing and rental assistance (i.e. Section 8), the housing programs that serve the lowest-income households. In addition to 34,000 federal public housing units and 128,000 Section 8 vouchers, Massachusetts also built and maintains 50,000 units of state-funded public housing and operates its own $35 million rental assistance program. Together, these programs house nearly 80,000 people. Only New York State begins to approach this level of commitment. New York has approximately 60,000 state public housing units, but has three times Massachusetts' population. Only a handful of other states have any involvement in either one of these state sponsored programs.

During the 1990s, state housing policy shifted in several respects. In part, these shifts reflected the state's dire financial circumstances in the early years of the decade. In part, they reflected a realignment in philosophy. First, state capital funds were concentrated on the preservation and modernization of the existing stock of state-aided public housing, rather than on the development of additional units. After an initial decrease partially necessitated by the need to repay $1.3 billion of "fiscal recovery bonds" floated to cover operating deficits during the state's fiscal crisis in 1990, state funding for public housing modernization was increased by 290% between fiscal year 1993 and fiscal year 2000. In addition, state funds to subsidize public housing operations have increased 47% since 1994. Recently, housing authorities have been able to undertake additional maintenance work by using newly available operating funds. These additional funds have become available, in part, because even though housing authorities have experienced increases in rental income because of the improved economy and increased numbers of tenants working as a result of welfare reform, the state has not reduced the subsidy dollars it makes available. DHCD has provided additional spending authority for housing authorities to implement a program that allows the painting of exteriors of buildings and common areas, the installation of air conditioning in the common areas of elderly housing developments, and a permanent increase in allowable maintenance expenses.

Second, the state's Chapter 707 program was curtailed beginning in 1990, partially in response to high costs – the program was the largest and most expensive program of its kind in the nation – and partially out of a legislative concern that excessive numbers of rental subsidies in some neighborhoods were inflating rents for unsubsidized tenants. In addition, some aspects of the program, such as the payment of landlords' claims for damage caused by subsidized tenants, were viewed to provide poor incentives. The 707 program was replaced in fiscal year 1993 by the Massachusetts Rental Voucher Program. That program's design included the reduction by attrition of mobile, tenant-based subsidies. The law precluded reissuing a voucher surrendered by a participating household. As a result, expenditures on the program were reduced each year to account for the decrease in the number of existing vouchers. That course was reversed in the fiscal year 2000 budget, which for the first time authorized reissuing surrendered MRVP tenant-based vouchers. In addition, even as the number of state-funded rental subsidies was reduced by attrition, the number of federally-funded Section 8 rental subsidies increased by 48% during the 1990s. More than 14,700 new Section 8 subsidies more than offset a reduction of 11,300 707/MRVP vouchers.

Finally, the state shifted the way it directly funds affordable housing development. Considerable resources had been devoted to the development of state-aided public housing. That is the most expensive way for government to expand the housing supply because it requires that the state initially to pay every dollar of development costs -- which are high because of the requirements surrounding public construction -- and then to pay ongoing, annual operating subsidies. In the 1990s, the state instead stressed leveraging its funds with other public and private funds to implement a more cost-effective method of creating low- and moderate- income affordable housing. The 1990s saw the authorization of new state funds for the Housing Innovations Fund and the creation of the Housing Stabilization Fund, the Capital Improvement and Preservation Fund, and the Facilities Consolidation Fund.

In addition, the decade saw the creation of the federal HOME program and the maturation of the federal Low-Income Housing Tax Credit program. The Low-Income Housing Tax Credit program began to realize increases in the private dollars it leveraged due to improving market conditions, program design, and management. In 2000, the Low Income Housing Tax Credit program is expected to leverage $73 in private investment for every $10 dollar tax credit allocation, compared to $50 of private leveraging for the same tax credit allocation in 1990. This new model also allowed the newly created housing to be privately owned and managed.

All of these programs established a competitive, as opposed to a rolling, application process that resulted in applications having a higher level of private investment in order to stay competitive.

In addition, while state spending on public housing construction decreased, funding for DHCD programs that leverage private investment for affordable housing development have *increased*. The result of these patterns of funding and shifts in emphasis is that the number of affordable housing opportunities[81] created from 1991 to 2001 increased to 34,599 from 24,419 in the previous decade.

[81] Creating an affordable housing opportunity includes producing or preserving an affordable housing unit or assisting a household with homeownership.

Action Agenda

The number and extent of federally and state-funded affordable housing programs in Massachusetts have created a large number of housing units and subsidies that allow low- and moderate-income people to pay varying levels of below-market rents. Nevertheless, they have not been able to arrest the increase in housing costs for renters and prospective homeowners across the income spectrum. The 1980s saw a number of affordable housing programs in Massachusetts. But even the combination of the SHARP, RDAL, and TELLER programs with ongoing regular MHFA lending for affordable housing, project-based development under Chapter 707, and more than $100 million per year of state spending for public housing development did not solve the systemic problems that once again have led to an imbalance between housing supply and demand in Massachusetts. And the scarcity of housing leads prices and rents to be driven up not only for relatively affluent households, but also for low-income households–including those with and those without subsidies. The scarcity of supply and especially of new stock attractive to middle and upper income households means that these households have needed to look to communities, neighborhoods, and buildings that had traditionally housed families and individuals of more modest means. South Boston, Jamaica Plain, and Somerville were once largely affordable communities. Triple-deckers once provided apartments for working families; now they increasingly become condominiums for professionals. The supply constraints in Massachusetts cause lower-income families and individuals to come into competition with more affluent households for scarce housing units. The result is entirely predictable: the specific low-income household is outbid, and the competition drives up prices in general.

There are two ways to address this particular situation. One is for the government to provide an affordable unit or a subsidy for the low-income family. The other is to free the private market to produce enough units for the market-rate household. Massachusetts does a great deal of the former, has done so tracing back to 1948, and has plans to continue using existing and new programs. Annually, the state and federal governments spend more than $1.3 billion in Massachusetts to subsidize the construction, rehabilitation, and operation of affordable housing developments and on rental assistance for low-income households. This figure does not include nearly $1.1 billion that departments in the state Executive Office of Health and Human Services spend annually to provide housing and related services to their clients. But that alone has not proved to be enough, especially in the current environment of high housing demand.

In 1999, new residential construction permits were issued for 18,967 housing units in Massachusetts, 3,510 of them in multifamily structures of two or more units. Also in 1999, state agencies approved financing for developments containing approximately 1,800 new housing units.[82] Approximately one-half of all multifamily production in Massachusetts involves government funding from a state agency. A 10% increase in overall housing production would have an effect on the Massachusetts housing supply equivalent to doubling government financing of new affordable housing development. Improvement of the operation of the private housing

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[82] DHCD reported approving funding for the production of 1353 new units, MHFA reported 444, and MHP reported 309. While these three figures total 2106, there is significant overlap between the three agencies, and 1800 is a generous estimate of the actual number of newly produced units. There is a lag between approval of funding in government programs and the issuance of a building permit, but the general levels of both and the relationship between them have been relatively constant over the last few years.

market can bring capital to bear for the expansion of the housing supply to a degree that government cannot match.

Even expanded government funds for affordable housing production will not necessarily result in large numbers of additional new units. Government funded housing, while sometimes able to obtain relief from many development barriers under Chapter 40B of the General Laws, still faces the costs imposed on development in general by the restrictive overall environment. In addition, these projects also can face the same kinds of costly delay and crippling uncertainty that private projects do as they work through local approval processes. The Massachusetts Housing Finance Agency currently has pending an elderly housing project proposal that dates back to 1993. While this length of delay is not typical, it is a worst-case example of the dynamic that discourages more development proposals.

The supply of housing available to the residents of Massachusetts has not kept pace with increased demand, and the result has been a rapid escalation in house prices and rents. High housing costs have made it more difficult for the poor and others of modest means to sustain or obtain their housing. The recent escalation of prices has made it unfeasible for too many families to buy their own homes. The disproportionately high cost of housing also threatens the Commonwealth's competitiveness and economic health by making Massachusetts less attractive to employers and workers.

It is imperative for the Commonwealth and its communities to address the need for housing. This must be accomplished by continuing the financial support for the preservation and development of affordable housing for low- and moderate-income households. But that alone is not enough. The state and its cities and towns must break through the bottleneck that keeps private development from keeping pace with demand.

The following lays out an agenda of some initiatives already underway and others that need to be launched to address the need for more housing in Massachusetts. These initiatives seek to help communities move forward through incentives, rewards, and a bargain where local aid is allocated to offset the incremental municipal costs resulting from new development. Together, these proposals offer new state resources to allow the development of housing for low-, moderate-, and middle-income households; show a new way to maintain the state's historic commitment to help house those with the greatest need; propose solutions to the unfortunate housing side effect of one of our greatest assets, the presence of our colleges and universities; and seek to assure that those who provide low-cost housing without government assistance can continue to do so.

Executive Order 418

Initiative: Continue to implement Executive Order 418 and expand outreach to encourage cities and towns to plan for and promote housing development.

Statutes are written and many policies are set at the state level, but Massachusetts has several centuries of history, a constitution, and laws that ensure local control of a wide variety of decisions, including most of the government decisions surrounding development. Town meetings or city councils adopt zoning ordinances. Local building inspectors enforce zoning and land use regulations, subject to appeal to local zoning boards of appeal. Local conservation commissions and their inspectors at least initially enforce state environmental laws and regulations, as well as any additional local regulations. Local public works and water departments and water and sewer districts enforce local standards for road, water, and sewer construction.

The way a community chooses to use its powers in these areas can have great impact on the amount and nature of development within its borders. While it is true that a community cannot cause development unless the marketplace makes it feasible, it is also true that a community can often stop otherwise feasible development – or at least significantly increase its cost – through burdensome local regulations or processes.

These local regulations account for as much as 50 percent of new housing costs. Examples of local contribution to the high cost of development include: arbitrarily high building standards, local inspectors who substitute their own standards for the established building codes, overly strict septic system rules which exceed requirements in Title 5, and restrictive zoning ordinances and bylaws such as large minimum lot sizes and low-density building requirements.

If done on a regular basis, impeding projects can introduce sufficient uncertainty about costs to make developers hesitate to develop in a community. Meanwhile, housing costs continue to increase for prospective new homeowners and for renters as housing supply fails to keep pace with demand.

To assist communities to reduce local barriers and help address the housing shortage, Governor Cellucci issued Executive Order 418 (E.O. 418) on January 21, 2000, directing the state offices of transportation and construction, housing and community development, and environmental affairs to help communities plan for future development by providing up to $30,000 in grants and technical assistance. Furthermore, E.O. 418 directed these agencies plus the state Department of Economic Development to give priority in awarding $364 million in discretionary grant funds to those cities and towns that take steps to increase the supply of housing.

Housing Certification

To receive priority for discretionary funding, communities need to gain housing certification through a process run by the state Department of Housing and Community Development (DHCD). The process requires the communities take proactive steps to encourage the development of housing affordable to individuals and families across a broad range of incomes. “Affordable” is defined in the executive order as ownership units that are assessed or valued at no more than the level that a household whose income is at or below 150% of the area median income could pay using 30% of their income, or rental units with rents that could be paid with not more than 30% of the income of a household at or below 100% of area median income.

Under E.O. 418, communities can choose from several different methods for improving the climate for housing development and can develop new techniques for their specific situations. The methods from which communities can choose range from holding open forums on the housing needs of the community, to identifying land suitable for affordable housing development, to forming local housing partnerships and trusts, to adopting incentive zoning provisions that increase density and broaden development options. The standard for certification will be raised in the second and third year to encourage continuing improvement. By year four, housing certification will depend on how much new housing is produced in the community. This will ensure E.O. 418 focuses on outcomes, not process.

Priority under E.O. 418 affects twenty different funding programs totaling more than $360 million in annual grants. For example, priority status will be awarded to communities for Public Works Economic Development grants, Community Development Action Grants, Sewer and Water Revolving Loans, and Community Development Block Grants. Housing-certified communities will receive roughly a 10% scoring bonus in programs that award over $340 million annually through periodic, competitive funding rounds. Only housing-certified communities will be eligible to apply for approximately $21 million per year awarded through grant programs with rolling applications (applications which are accepted continuously, rather than in periodic funding rounds).

Community Development Plans

Over a two-year period, cities and towns in Massachusetts will be eligible under E.O. 418 to apply for up to $30,000 each in grants or in-kind services to complete community development plans. The plans will focus on developing housing for families and individuals across a broad range of incomes while balancing the need for economic development, transportation improvements, and open space preservation. Community development plans are intended to be image-based blueprints for cities and towns that identify their future growth in four core areas: housing, commercial and industrial development, transportation, and open space/resource protection. Growth requires that communities balance these four core areas that are critical to improving quality of life and preserving community character. Elements of the plans, which address how the community will accomplish its development objectives, include at a minimum:

- location, type, and quantity of new housing units, including housing affordable to individuals and families across a broad range of incomes;
- location, type, and quantity of open space to be protected including identification and prioritization of environmentally critical unprotected open space, land critical to sustaining surface and groundwater quality and quantity, and environmental resources;
- location, type, and quantity of commercial and industrial economic development; and
- location and description of recommendations for improvements to transportation, e.g., bridge work, road drainage systems, revised intersections, public transit, and alternative modes of transportation.

Once a community is eligible for the planning grant, it will receive a customized guidebook that is made up of two parts. The first section of the guidebook is uniquely designed for each community. This segment contains data specifically related to the condition of housing, transportation, the economy, and the environment within that community. The second portion of the guidebook is identical for all communities, and it provides a discussion of planning tools and best practices. Combined, these two complementary components will help communities prepare their own development strategies that tailor general planning principles to their own specific needs.

If a community has recently completed a master plan covering those areas, the $30,000 may be used to augment specific areas of its plan or on additional pre-implementation preparation.

By emphasizing planning in addition to housing certification, E.O. 418 does not try to force communities to accept development at odds with their unique characters, but rather allows communities to self-determine how they will meet E.O. 418's goal of increasing housing supply. The executive order recognizes different market conditions and individual community circumstances, but also presumes that every community can make a contribution to ameliorating our current housing problem by devising solutions that are responsive to local and regional needs.

Executive Order 418 has already had a positive impact at the community level. In communities across the Commonwealth, E.O. 418 is sparking discussion about local barriers to residential construction, especially development that is affordable to people with a wide range of incomes. The Department of Housing and Community Development reports an increase in the number of inquiries they have received regarding affordable housing development. In addition, many communities have specifically requested more information about E.O. 418 and municipal and planning groups have requested presentations on the executive order and affordable housing. Articles have also appeared in local papers such as the Bedford Minuteman and the Berkshire Eagle that discuss the local implications of the executive order.[83]

Continued outreach and training are essential components to ensure the effective implementation of E.O. 418. To follow up on his executive order, the Governor will host a *Conference on Housing* in October that will bring together many housing professionals and communities to develop an array of successful housing models that are responsive to a variety of housing markets and local conditions. This conference will be followed by a series of symposia that will explore in more detail specialized components of housing development (e.g., single person housing, planning and zoning, supported housing). In addition, technical assistant grants are available to communities through the Massachusetts Housing Partnership Fund.

Challenging Communities to be Part of the Solution

E.O. 418 is an innovative effort to increase the supply of housing across the Commonwealth. Achieving this goal depends on the cooperation and political will of local communities. To the extent communities fear increasing development will have negative effects, E.O. 418 provides priority access to resources like open space grants, transportation funding, and Massachusetts Water Pollution Abatement Trust loans that can help a community manage those effects. For

[83] "Town Drafts Response to Affordable Housing Needs" *The Bedford Minuteman* (July 19, 2000). "Housing Shortage Puts Squeeze on Berkshires" *The Berkshire Eagle* (July 17, 2000).

instance, a Water Pollution Abatement Trust loan can fund a sewer system, eliminating the need for larger lot sizes that septic systems require. Strategic purchases of open space can preserve a community's character far better than continuous large lot development. Thus, E.O. 418 challenges communities to address the drawbacks of development directly, rather than hiding behind inefficient and ultimately ineffective land use regulations and other regulatory barriers.

Through the incentives created under the E.O. 418 housing certification process, the resources to which it provides access, and the ongoing technical assistance offered, the Commonwealth can help local communities take up the challenge of improving the housing situation in Massachusetts.

Special Commission on Barriers to Housing Development

Initiative: Appoint a special commission to recommend statutory, regulatory, and operational changes to reduce unneeded barriers to housing development.

In preparing this report, the Executive Office for Administration and Finance and the Department of Housing and Community Development convened groups to discuss several aspects of the housing supply problem in Massachusetts. Some specific recommendations arising from this process are being proposed or implemented by the Administration and are discussed later in this report. Executive Order 418 gives cities and towns an incentive to reduce the local barriers to residential construction, but it may also be necessary to effect statutory and regulatory changes to move forward most effectively. But it is also necessary to expand the scope of the discussion in order to successfully address not only the systemic problems, but also the attitudes and perspectives that lead to the state's housing supply problem.

To engage a broader spectrum of interested parties in the formulation of strategies to address the state's housing problem, the Cellucci-Swift Administration will establish a special commission on barriers to housing development. The commission and its working groups will systematically review government-imposed barriers to residential development and recommend to the Governor specific legislative, regulatory, policy, and operational changes beyond those discussed in this report that are needed to remove unnecessary state and local barriers. In relation to the initiatives discussed in this report, the commission will examine and make recommendations regarding zoning and land use controls, local enforcement of building and related specialty codes and the implementation of expanded training for local officials, and local septic system standards exceeding those prescribed by Title 5

The commission will submit their recommendations to the Governor and Lieutenant Governor by June 30, 2001.

Housing Supply Incentive Program

Initiative: Revise the provision of local aid to reflect increased municipal costs resulting from housing development.

Even for communities who accept the challenge presented by Executive Order 418 and look for ways to increase their housing supply, there remains a significant disincentive to residential development. The on-going costs new development imposes on local budgets, particularly the education costs, cause many communities to resist the construction of new housing.

To address these costs, Governor Cellucci included in his fiscal year 2001 budget proposal the Housing Supply Incentive Program, funded at $47 million per year. This program would pay the difference between what a community could expect to receive in tax revenue from new development and the costs of educating the school children anticipated to result from such development. The formula for distributing this money is based on estimated levels of additional funding needed to meet the foundation funding level called for in the Education Reform Act of 1993 for the increased enrollment expected due to new single-family and multifamily units (see Appendix B). Even though the formula determines the allocation based on anticipated education expenses, localities could use the funds for any government purpose.

Houses with low assessed values and, as a result, low expected tax revenues, would earn more aid than more expensive ones. Apartments with two or more bedrooms, which are more likely than one-bedroom apartments to house families with children, would earn the highest amount of aid. In this manner, the program would provide an incentive for multifamily development, which both provides much-needed rental housing for those who cannot afford to own houses and creates more dense development that does not contribute to urban sprawl.

The funding from the Housing Supply Incentive Program for new development in a given year would represent a ten year commitment, so that cities and towns would know that the on-going costs imposed by development would have a long-term offset. After ten years, that stream of funds would be available either for continuation of the program or for other Commonwealth priorities, as indicated by conditions at that time.

The Housing Supply Incentive Program was not included by the legislature in the state's fiscal year 2001 budget. It still needs legislative approval, and it should be pursued once again in the next legislative session. Communities have responded to the fiscal disincentive to allow residential development; we expect they would also respond to the removal of that disincentive. In so doing, they will put the power of the private housing market to work, building far more units than public programs could conceive of building.

How the Program Works

The Housing Supply Incentive Program would be funded by redirecting 10% of the local aid distributed through the Additional Assistance account each year, or about 1% of the $4.8 billion the state annually distributes in local aid. The proposed program would be funded from an existing local aid account. There are two reasons to fund the program in this manner. First, using an existing funding source means that money for the program is already in the state budget base. This assures communities that if they make changes in zoning laws today or otherwise encourage housing construction, funds will be available to offset the costs of development that occur three or four years later. Second, distribution of local aid according to the proposed new program is more fair than using the current formula, because it recognizes real, new municipal costs, rather than relying purely on inertia for its rationale.

The Additional Assistance account was established in 1977 as a $30 million program and expanded rapidly throughout the 1980's, primarily to offset the effects of Proposition 2½. Since 1992, it has been frozen at its then-existing levels for the 159 of the state's 351 communities that receive finds from this account. Due to the several manipulations in the Additional Assistance formula prior to 1992, changes in relative community needs since then, and the comprehensive revision of Chapter 70 state aid for education under the 1993 Education Reform Act, the formula no longer allocates funds based on any recognizable definition of need. Several wealthy communities such as Belmont, Newton, Lincoln, and Sudbury receive substantial sums annually from the formula, while less affluent cities including Lawrence, Leominster, and Attleboro receive little or no funding. For those communities that are truly needy and currently receive funding from the Additional Assistance account, the Housing Supply Incentive Program includes a scaled, needs-based hold harmless provision.

The Housing Supply Incentive funding formula was developed based on regression analysis of the impact of housing growth on school enrollments. The regressions indicated that new single-family homes in Massachusetts increase foundation enrollment by 0.49 students on average, while new multifamily units increase enrollment by 1.27 students in communities above the 10% affordability threshold as defined by Chapter 40B of the Massachusetts General Laws and by 3.17 students in the city of Boston. The formula applied these coefficients to statewide average education expenses per pupil or the per pupil foundation budget of the community, whichever was greater, to determine the expected education costs related to new development in a community. To the extent that expected education costs of each new unit exceeded the anticipated tax revenue from that unit, the formula provided the community with the difference. This means that, depending on a locality's foundation budget, single-family houses of up to $220,000 in value and all multifamily units would generate additional local aid for the community.

Multifamily units in localities below the 10% affordability threshold did not have a statistically significant effect on enrollment. The hypothesis for this negligible effect in primarily suburban towns is that multifamily units that are being built in such communities are targeted at households without school-age children, such as seniors or singles. To ensure suburbs had an incentive to build multifamily units suitable for families, the formula uses the statewide coefficient on multifamily units of 1.11 for all multifamily units with at least two bedrooms built in localities below the 10% affordability threshold. The single-family coefficient of 0.49 was applied to all multifamily units with fewer than two bedrooms in all communities.

Data on the assessed values of new residential construction completed in 1998 and assessed for taxes in 1999 (the most recent available data at the time) were requested from all 351 cities and towns and successfully collected from 310 of them. The remaining 41 cities and towns accounted for only 5% of the average number of building permits issued for new residential construction annually between 1997 and 1999, according to U.S. Census data. The survey data indicated that 13,465 new single-family and 4,595 new multifamily housing units were completed in these 310 municipalities in 1998.

Using the estimates of enrollment growth developed as part of the program, the Executive Office for Administration and Finance estimated that the statewide average annual incremental school cost attributable to this new development amounted to $28 million. The remaining $19 million of the program's $47 million budget would be disbursed through a hold-harmless provision that would distribute funds to current recipients of Additional Assistance whose continuing need is demonstrated by how far below the state average their adjusted equalized valuation per capita is.

Providing Tax Benefits for Affordable Housing Development

Initiative: Expand the Economic Development Incentive Program to promote housing development.

Housing development is an expensive proposition anywhere, and that is especially true in Massachusetts.

It is important in Massachusetts to spur the private development of housing that is affordable to families and individuals across a wide range of incomes. Executive Order 418 and the Housing Supply Incentive Program seek to encourage local communities not to unduly restrict the private development of housing. But even if governmental impediments are lifted, new housing affordable to those of modest means is not feasible without some form of financial assistance.

The Commonwealth funds or administers a wide variety of grant and low-interest loan programs to help make the development of affordable housing feasible. The state's Department of Housing and Community Development awards nearly $100 million annually for the development and preservation of privately-owned affordable housing, and its affiliated quasi-public housing agencies provided $160 million in financing for affordable housing projects in 1999. Since then, the Governor and the legislature have approved two new programs, the state Low Income Housing Tax Credit program and the Affordable Housing Trust, that together will over the next five years commit $200 million in additional state funds for affordable housing.

There are other methods of providing financial aid and incentives for housing development, including affordable housing. The Economic Development Incentive Program (EDIP) offers one alternative model. Recognizing this, Governor Cellucci and Lieutenant Governor Swift on June 22, 2000 filed H. 5285, titled "An Act Creating a Pilot Expansion of the Economic Development Incentive Program to Include Affordable Housing Development Projects." The proposed act would simply extend the benefits currently available under the Economic Development Incentive Program to the development of affordable housing. The bill would implement the program on a pilot basis for five years or 200 projects, whichever comes first, providing up to $2 million per project. Expenditure on the EDIP is estimated at approximately $4 million in new money each year. The legislature's Joint Committee on Housing and Urban Development committed the bill to study, and it was not taken up by the House of Representatives or the Senate during the 2000 legislative session.

The EDIP is a highly successful program that spurs private investment in projects that provide jobs in priority areas of the state. An employer planning a job-producing project in one of the state's designated Economic Target Areas (ETAs)[84] can apply with the city or town where the project is located for Project Certification under the EDIP. If the state's Economic Assistance Coordinating Council approves an application, the project can obtain the following tax benefits:

- eligibility for a 5% tax credit on qualifying investments made in plant, equipment, and other tangible, depreciable assets over the term of the project's certification, which can be five to twenty years;

[84] The project need not be in an economic target area if it is certified by the state's Director of Economic Development certifies it as an "exceptional opportunity."

- a tax deduction for 10% of costs incurred to rehabilitate an abandoned building; and
- a municipal tax incentive, consisting of either
  - a special tax assessment, which is a negotiated phase-in of local property taxes over five to twenty years on the value of the real estate owned or leased by the project; or
  - tax increment financing (TIF), which serves to pass tax savings on to property owners for use in project development, while ensuring that the development risk is borne by those parties as well. TIF allows a property tax exemption based on a percentage of the value added through new construction or significant improvement over a period of five to twenty years. The additional real estate taxes generated by the increase in assessed value are then allocated by percentage to one or more of three categories, each of which may change from year to year: exemption from real estate taxes, payment of real estate taxes, and payment of a betterment fee in lieu of real estate taxes to finance related infrastructure.

In addition to facilitating new development, the EDIP is also instrumental in reusing underutilized or abandoned sites. This kind of "infill" development not only provides space for business or housing use, but it also revitalizes an area that would otherwise be blighted, and it also helps to contain urban sprawl. When the infill development occurs in a "brownfield" area that has some degree of environmental contamination from a previous use that can be remediated and made useful once again, the benefits are multiplied.

Expanding the EDIP to incorporate housing development could facilitate development of new housing in undeveloped areas. It could also be used to convert obsolete commercial and industrial space to residential use. Or it could also be used in connection with more traditional use of the EDIP for business expansion to help spur mixed-use development. One example of such a use is the revitalization of downtown areas. An expanded EDIP could be used to develop a combination of retail or commercial space and housing. Housing developed or renovated in a downtown area can be a key element in restoring its vitality.

In keeping with a long-standing principle that providing affordable housing to "low-income" households using public funds serves a public purpose, the tax benefits in an expanded EDIP should be available in proportion to the units in an affordable housing development that are occupied by income-eligible households. Under the Cellucci-Swift administration's bill, at least 25% of the units in a development would be reserved for households at or below 80% of the area median income, the traditional state standard for affordable housing. Another 25% of units would initially be either rented to households between 80% and 100% of area median income or sold to households between 80% and 150% of area median income. The upper limits for this second tier of affordable units are consistent with those recognized in Executive Order 418.

For several reasons, extending the EDIP is an attractive method to promote the development of housing affordable to households across a broad range of incomes. The EDIP already exists, so it could be made available for housing development quickly using an existing administrative and governance structure. The development community is familiar with how the program works, so there would not be a need for an extensive education process. It is easily accessible to developers working in the state's economic target areas, so it may encourage developers who have not previously done so to develop affordable housing. Finally, the EDIP process places communities in the driver's seat, so they can put forth development projects that meet their local needs. In this manner, it complements Executive Order 418. An expanded EDIP would provide many cities and towns with a tool they can use to help solve the housing supply problem in Massachusetts.

Unlocking State Assets to Help Provide Housing

Initiative: Expedite the disposition of surplus state-owned property to provide sites appropriate for housing development.

The inadequate availability of land suitable for development is one of the fundamental problems that depresses housing production in Massachusetts. Meanwhile, the Commonwealth's departments and agencies own property across the state that is neither being used nor is it needed to carry out their functions. Rather than lying fallow indefinitely, parcels of this land that are suitable for housing development should be made available for this purpose. This valuable asset of the Commonwealth should be unlocked and committed to productive use.

In June 22, 2000, Governor Cellucci filed H. 5286, titled "An Act Facilitating the Development of Underused Facilities and Properties for Housing in the Commonwealth." The bill was referred to study by the legislature's Joint Committee on Housing and Urban Development and was not taken up by the House of Representatives or the Senate during the 2000 legislative session.

The Cellucci-Swift Administration's bill streamlines the disposition process for unneeded parcels of state property that can be used for housing development. The streamlined process could save a year or more compared to the current process. Under the proposed law, the state's Division of Capital Asset Management and Maintenance (DCAMM) would dispose of the property either to the Massachusetts Development Finance Agency (MassDevelopment), which would then market it for development, or directly to private developer. The proposed legislation would permit DCAMM to do this without an act of the legislature for each disposition. MassDevelopment would reinvest the net proceeds they realize from sales to remediate environmental hazards and to finance other costs on subsequent sites through the use of a revolving fund. In this manner, the proposed program would create a source of funds to clean up contaminated state land.

Property disposed of under this act would be subject to reuse plans approved by affected communities. Reuse plans for parcels transferred under this law could include open space or commercial development, but they would be required to include a significant residential component.

Before this bill was filed, the Commonwealth undertook a review of land that might be appropriate for disposition under the proposed new process. In short order, DCAMM and the Massachusetts Highway Department were able to identify nearly 1,000 acres of potentially available land. Some of this land was in stand-alone parcels. Much of it was on the sites of functioning state facilities where there is currently unused space for which there is no plan for future use.

In the future, the state should:

- continue to inventory unneeded state real property on a regular basis, and actively assess the suitability of entire sites and portions of sites for housing development;

- implement more efficient methods of converting surplus state property to productive use by streamlining the disposition process; and

- develop mechanisms to publicize the inventory of surplus state property and to make it broadly accessible by putting it online.

By identifying and making available state property that is suitable for development, the Commonwealth can make use of dormant assets and contribute to improvement of the housing problem.

Improving the Climate for Rental Housing

Initiative: Protect stability in rental housing by enacting a requirement that tenants place rent in escrow if they withhold it claiming substandard conditions.

When one thinks of housing affordable to people of modest means, one often thinks first of large, publicly owned or assisted apartment developments. Massachusetts has tens of thousands of this kind of affordable housing unit, and they serve a vital need. But many low-income households live without government assistance in privately owned properties that have low rents simply because of their location, condition, or position in the market.

One way that people with low incomes are able to afford homeownership is to buy a small apartment building and rely on the income from the two or three rental units to pay the mortgage that they otherwise would not be able to afford. These owners rely on a steady rent stream to operate, maintain, and pay the mortgages on their properties. Long and unexpected interruptions in rent payments can imperil their financial health and, in doing so, threaten the availability of housing.

Discussions with representatives of small landlords, with real estate groups, and with municipal officials have indicated that the current operation of tenant-landlord law in Massachusetts discourages some owners of rental properties from renting their apartments and contributes to abandonment of rental properties. In this manner, the status quo can contribute to the state's rental housing supply problem.

One law that has been suggested to be particularly vulnerable to abuse is the rent withholding provision found in Chapter 239, section 8A of the Massachusetts General Laws. Under Massachusetts law, a landlord is required to provide a unit that meets the requirements of the state sanitary code, and the obligation to do so creates a "warranty of habitability." If the existence of code violations breaches this warranty of habitability, a tenant who withholds rent is entitled to assert a defense against eviction based on this breach. This is an important safeguard for tenants against landlords who are not providing adequate housing. Unfortunately, tenants can also abuse this right, even if their apartments do not have substantial code violations. It is not unusual for tenants to contest evictions for non-payment of rent by asserting habitability defenses and remaining in their apartments without paying rent for several months before the eviction case is concluded.

The current system can be inequitable in its treatment of landlords, even those who ultimately prevail in court. As it stands, Massachusetts law allows but does not require a court to order a tenant to place an amount equal to the "fair rental value" of his apartment in escrow. The fair rental value of an apartment is its agreed-upon rent or some lesser amount that reflects any deficient conditions. A court can order rent to be placed in escrow only after a hearing on all the facts of an eviction case, which occurs no earlier than 32 days after non-payment -- and later if, as is often the case, a landlord does not immediately serve a notice to quit when a tenant fails to pay rent on the due date. Because the court is required to hold a substantial hearing prior to ordering the tenant to escrow his rent, courts seldom make use of this rent escrow provision.[85] Judges can and do use their equity powers to order tenants to put money into the court if they default or request a continuance.

By the time the matter is adjudicated, several months' rent may have been withheld, and even if a landlord prevails and a court orders that the tenant pay back rent, funds are often not available to satisfy the judgment of the court. The tenant loses his right to remain in the unit if he fails to pay the amount of back rent ordered by court, but the landlord can lose significant rental income in the meantime. In addition to lost rent, the landlord must pay substantial legal fees as well as other costs related to the physical eviction of the tenant.

In order to address this issue, the Massachusetts Department of Housing and Community Development convened meetings with government agencies and advocacy groups representing tenants, property owners, real estate agents, and the banking industry. The goal of these meetings was to discuss the nature and extent of the problem and actions state government could take to make the lawful withholding of rent more about the condition of an apartment and less about missed payments. While parties did not agree on the conclusions that should be reached, information was provided that informed future steps.

To address the inequities in the current system, the Cellucci-Swift Administration will file a bill in the 2001 legislative session to require tenants to escrow their rent if they withhold it due to deficient conditions. The bill will protect landlords against tenants who abuse the habitability defense while providing adequate consumer protections for tenants with bad landlords. Requiring tenants to place their rent into escrow in order to assert a habitability defense will reduce the number of fraudulent claims of code violations. Putting rent into an escrow account will show that the tenants are willing to make a good faith effort to maintain their tenancy, and it will also help ensure that funds would be available to pay to the landlord the amount of back rent the court orders.

By requiring the tenant to escrow rent in order to assert this defense against eviction for non-payment of rent, the legislation reduces the ability of a tenant to assert an after-the-fact claim of deficient conditions to introduce delay as a means to avoid paying rent. Under the proposed legislation, a tenant would be required to notify his landlord that he is withholding rent and why he is doing so. He would then put aside in an escrow account or a separate bank account the amount of his contract rent, less necessary and documented expenses incurred due to the claimed deficient conditions.

At the same time, the proposal includes provisions to adequately protect tenants from abuse by landlords. To ensure that the tenant knows and has the opportunity to meet his obligations under the law, the legislation requires that in order for an owner to obtain the protections available under the new legislation, the landlord must notify a tenant who has failed to pay rent that that he is required to escrow withheld rent. The Administration also recognizes that tenants may incur additional expenses due to the existence of code violations in their apartments. Where this is the case, the tenant may reduce the amount of rent he pays into escrow by the amount of

[85] Interviews with Harvey Chopp, Boston Housing Court Administrator; Stephen G. Carreiro, First Assistant Clerk Magistrate at the Southeastern Housing Court; and Michael J. Finucane, First Assistant Clerk at the Waltham District Court.

documentable out-of-pocket expenses incurred for such purposes. Several other safeguards beyond the right to withhold rent currently help protect the rights of tenants. These safeguards would remain unaffected by this legislation. They include a tenant's right to seek the assistance of the board of health, the right after sufficient notice to effect repairs and offset the cost against rent, the right to file a criminal complaint, the right to sue the landlord for money damages, and the right to file a counterclaim for money damages if the landlord seeks to evict him.

A further goal of the legislation to be proposed is to encourage landlords and tenants to communicate with each other and to settle such matters without the time and expense of litigation. To that end, the legislation will include provisions that would allow and encourage tenants and landlords to work out their disputes before court action is necessary.

Many landlords and tenants do not fully understand their risks and responsibilities. Education and outreach are key components of any effort to improve their ability to resolve conflicts without government involvement. To that end, tenants and landlords will be able take advantage of newly formed Consumer Education Centers funded in the fiscal year 2001 budget in order to better understand their rights and obligations. These centers will also help mediate between landlords and tenants without court involvement.

It is important to remove the element of surprise and after the fact recrimination that occurs too often under current tenant-landlord law by requiring all parties to be clear about their actions and intentions in advance. The law must be balanced to provide tenants with the protections to which they are entitled as consumers and landlords with the protections to which they are entitled as property owners. The Administration's bill will strike this balance and help ensure that landlords do not hold their rental properties offline for fear that abuse of the laws will leave them with an unreliable source of rental income.

Improving the Regulatory Environment for Development and Construction

Initiative: Reexamine the implementation of state regulations and policies that affect housing construction and development.

Beyond the land use and zoning restrictions discussed earlier, additional regulations can impede or increase the cost of housing construction. Of particular importance are building and related specialty codes and environmental regulations such as Title 5, both with respect to the regulations themselves and to the way they are enforced through local permitting processes. The Commonwealth will take steps to eliminate any excessive upward pressure that the structure, interpretation, or enforcement of these regulations may be placing on the cost of housing construction. Such steps will be taken in a manner consistent with promoting essential public health, public safety, and environmental protection goals.

Building Codes and Related Specialty Codes

Because there are numerous boards and state agencies independently promulgating the codes that regulate building construction, the Commonwealth will sometimes put into place regulations that are conflicting or duplicative. For the most part, this may be inadvertent and due to the large number of regulations and statutes related to the construction and rehabilitation of buildings. To address this issue, Governor Cellucci will file an executive order to prevent, identify, and resolve conflicting and duplicative regulations related to building construction and rehabilitation. Specifically, the executive order will establish a team that will address the issue of conflicting and duplicative codes. The team will consist of representatives from state agencies that deal with regulations relating to buildings and structures. By reviewing all proposed regulatory changes, the team will identify and resolve potential conflicts prior to the submission of the proposed regulation. In addition, the team will resolve any code conflicts or duplications that are discovered during the code implementation process.

Although it is the Commonwealth's responsibility to promulgate many of these codes, local building and fire prevention officials and local plumbing, gas, electrical, and health inspectors are responsible for their interpretation and enforcement. These local officials, despite good intentions, too often impose unduly restrictive building requirements upon builders due to a lack of appropriate training opportunities. This, in turn, places an upward pressure on housing costs.

In addition, there is often no practical recourse when local inspectors or safety officials fail to act expeditiously or make determinations that a property owner, builder, or tradesperson believes to be incorrect. Builders and tradespersons working in a community must rely on local officials to approve their future work, so they are reluctant file complaints or appeals, even when an administrative process exists. Property owners similarly acquiesce rather than seek redress so as not to imperil future approvals of their specific projects.

A final set of impediments to cost-effective construction are caused by formally-imposed requirements that are beyond a locality's legal authority. Building requirements (as opposed to site requirements) imposed through local approval processes under the Subdivision Control Act (see page 21) are an example.

In order to ensure consistent and appropriate enforcement of regulations relating to buildings and structures, Governor Cellucci and Lieutenant Governor Swift will call for a working group of the Special Commission on Barriers to Housing Development to design an expanded state-funded training program for local building and fire prevention officials, local plumbing, gas, electrical, and health inspectors, builders, and developers. Such a program will include training that would minimize the misinterpretation of state codes. Some of the training sessions will be designed to include the joint participation of local building and fire prevention officials; local plumbing, gas, electrical, and health inspectors; state regulators; and representatives from the residential development industry. Recommendations for the design and funding of this program will be determined by December 2000, in time for consideration in the fiscal year 2002 budget.

In addition, the working group will recommend mechanisms to ensure that local officials involved in inspection of approval of construction have appropriate oversight and accountability so that inspections and approvals are consistently timely and appropriate. Areas to be examined include licensure processes to deal with complaints and administrative appeals mechanisms for local inspectors' and safety officials' decisions.

Finally, the working group will review the formal local imposition of building requirements without legal authorization. The group will determine the prevalence of such requirements and, if warranted, recommend corrective action.

Title 5

Discussions with representatives of the residential development industry indicate that another source of expense and delay in housing development is caused by the local enforcement of Title 5 (310 CMR 15), the state regulation governing on-site subsurface sewage systems, including septic systems. The state Department of Environmental Protection (DEP) revised and tightened Title 5 of the State Environmental Code in 1995. Title 5 calls for existing systems to be inspected before property is transferred and, if they fail, to be upgraded within two years. New construction must also comply with the stricter protection standards.

Primary enforcement and regulatory responsibility rest with local boards of health under Title 5, though DEP is involved in approving certain alternative technology and variance requests. The standards contained in Title 5 were based on extensive scientific analysis and are sufficient to provide the needed level of resource protection under most conditions. Recognizing that there are varying conditions across the state, however, the code allows communities to establish local bylaws that are more stringent than Title 5, and 125 communities have provided notice to DEP that they have adopted such bylaws. Local soil and percolation conditions may indeed necessitate stricter requirements. In some cases, however, a community wishing to restrict residential development could effectively do so, or at least make it more expensive, by adopting excessively strict requirements for septic systems. In addition, a local board of health might adopt an unnecessarily tight standard as a result of an inaccurate analysis of conditions or technology. DEP indicates that some communities may have adopted local bylaws more stringent than Title 5 that may not have their foundation in science.

An additional aspect of Title 5 implementation that may make compliance more costly than necessary is the local certification of septic system installers. Only installers certified by the local board of health may install a septic system in a community. This limits the number of contractors available to install septic systems in any city or town, reducing competition and potentially driving up cost.

Many involved in real estate development believe that the manner in which Title 5 is being implemented in many communities has erected a barrier to development. They have indicated that more burdensome than the expense required by the basic requirements of Title 5 is the variation in local application and the existence of additional local standards. These local bylaws have imposed direct costs, as well as uncertainty and delay that have significant costs of their own. Where conditions dictate more stringent standards, the benefits of such bylaws may outweigh their costs. In other communities, an environmental protection code intended primarily to protect water supplies can be misused to restrict land use that would otherwise be allowed.

The issue bears further analysis. The Governor's special commission on barriers to housing development (see page 71) will be charged with examining the adoption of standards in excess of Title 5 and the enforcement of Title 5 and local septic system bylaws. With the assistance of DEP, the commission will determine the frequency with which local standards are stricter than what is required for scientifically valid environmental protection. The commission will recommend steps, including regulatory changes, that would ensure that on an ongoing basis, local requirements beyond those in Title 5 are imposed only when scientifically justified. The commission will review potential approaches to reducing the barrier to development caused by overly strict septic system requirements, up to and including uniform application of the statewide code, with communities required to demonstrate to DEP's satisfaction that any new requirements beyond those in Title 5 are necessary on a technical and scientific basis. The commission will also recommend how existing local requirements that exceed those in Title 5 should be addressed. Finally, the commission will consider improvements to the process for certifying septic system installers. The commission's findings regarding changes to septic system requirements will be included among its recommendations to the Governor and Lieutenant Governor by June 30, 2001.

In addition, DEP will evaluate its training and outreach efforts to determine if they should be expanded or intensified. As part of this process, DEP will develop a plan for targeted outreach and training to communities that may have adopted needlessly restrictive local requirements.

Building, safety, and environmental codes are necessary to the protection of public health, public safety, and the physical environment. Nonetheless, they can be applied in a manner that unnecessarily burdens housing development, either inadvertently or by design. In each case, state regulations can be expanded upon and are enforced at the local level. Local decisions determine the effect that the regulations have on development. State agencies must work with their local counterparts to ensure that the protections intended by these codes are effectuated without unintended development restrictions.

Single Person Housing

Initiative: Facilitate the development and rehabilitation of housing appropriate for and affordable to low-income, single person households.

Single individuals once had access to a number of low-rent housing options, including single rooms with shared bath, kitchen, and living space, often referred to as single room occupancy units. Over the past several decades, the number of these options has declined. Between 1965 and 1985, Boston experienced a 96% drop in single room occupancy units, the largest drop in the country.[86] The minimum housing standard that people find acceptable has risen over time and many now believe that studios and small one-bedroom apartments are more appropriate for many single individuals, but the availability of this type of housing is also limited and expensive for those with low levels of income. Many of the Commonwealth's homeless shelter providers have suggested that a lack of low-cost rental housing for single adults has contributed to the growing number of homeless individuals.

In recent years, the Commonwealth has been an active lender of funds for the development of housing for single persons. However, within the context of the Commonwealth's current housing shortage, there continues to be a deficiency of housing suitable for low-income single persons. To address this lack of low-cost housing options for single individuals, the Executive Office for Administration and Finance convened a working group to explore ways to support the development of such housing. The group included representatives from the Commonwealth's housing agencies, quasi-public housing agencies, and state government agencies within the Executive Office of Health and Human Services. The working group determined that efforts to encourage single person housing should consider:

- the need for gap financing;
- the cost of services;
- inflation;
- management challenges; and
- the needs of the community.

Taking these key issues into account, the working group agreed to implement the following initiatives designed to encourage the development of housing affordable to low- and moderate-income single persons.

A. *Reserve Funding and Project-Based Vouchers for the Development of Single Person Housing.*

The Department of Housing and Community Development (DHCD) will reserve:

[86] "Setting Domestic Priorities," The Brookings Institution, Washington, D.C., 1992.

1. Funding for 75 to 100 units of single person housing under the "development model" of the Individual Self Sufficiency Initiative (described above). Funding for such units will be reserved until December 31, 2000 for regional non-profit organizations who are interested in pursuing gap financing for properties that they or other interested private investors would own.

2. 100 project-based section 8 vouchers for single person development projects. The guaranteed revenue stream provided by these vouchers will help developers secure development loans and grants that could be used in concert with other funding. DHCD will commit up to 100 Section 8 project-based vouchers to a Single Person Housing Initiative and is prepared to issue Request for Proposals (RFP) to interested rental property owners. Eligible units must be in need of a minimum of $1,000 of rehabilitation work necessary to bring the units up to federal and/or state housing codes. Special consideration will be given to proposals that have previously secured commitments for funding to make the project feasible. Additional consideration will be provided to proposals that demonstrate a commitment to a social services component. Eligible single households must have incomes below 50% of the area median. Section 8 voucher authority is provided in one-year renewable increments.

B. Institute an Education Program on Single Person Housing for Developers, Communities, and other Interested Parties.

1. As part of the "Governor's Conference on Housing," scheduled for October 5, 2000, the Governor will sponsor a panel discussion on single person housing. Panel members will include representatives from the Commonwealth's public and quasi-public housing agencies and human services agencies. To an audience of housing professionals, municipal officials, for-profit and non-profit developers, and public and private lenders, the presenters will describe examples of non-profit and for-profit single person housing developments, highlighting those that have not only effectively met the needs of their respective communities, but are also considered assets in their neighborhoods. Discussions will include descriptions of best practices in terms of financing packages, management practices, and service plan models.

2. The Department of Housing and Community Development will sponsor a Symposium on Single Person Housing in January or February of 2001. To an audience of housing professionals, municipal officials, for-profit and non-profit developers, and public and private lenders, representatives from the Commonwealth's public and quasi-public housing agencies and human services agencies will present detailed information about funding available for single person housing development and services, financing resources, and debt underwriting requirements.

   The symposium will make available loan term sheets, program guidelines, and other materials specific to different financing resources and provide detailed information regarding the timing and process of applying for financial resources. In addition, the symposium will provide information about contact persons for each resource and how to follow-up for further information.

3. The Department of Housing and Community Development will coordinate the preparation of materials regarding single person housing to be made available at the Governor's Conference on Housing and the subsequent Symposium on Single Person Housing. DHCD will prepare information packets by consolidating its own materials with information it receives from the quasi-public housing agencies and the appropriate human service agencies. The department's Division of Private Housing will make these informational packets available to developers upon request beginning October 5, 2000. DHCH will also ensure the accuracy of the materials by collecting and consolidating all pertinent information on a regular basis.

C. Identify and Address Barriers to the Effective Use of the Facilities Consolidation Fund for the Development of Single Person Housing.

The Department of Housing and Community Development will identify and address barriers to the effective use of the Facilities Consolidation Fund for the development of single person housing. For example, DHCD will explore the possibility of supporting legislation that would address the reasons why developers appear to have limited interest in the Facilities Consolidation Fund program (described above). Legislation that improves some of the design elements of the program may make the Fund more useful and encourage more lenders to participate with the Department of Housing and Community Development in creating single person housing for clients of the Departments of Mental Health and Mental Retardation. A variety of potential legislative changes should be examined and discussed with housing developers. For example, possible changes to explore may include but not be limited to: (1) eliminating title reversion language; (2) bringing the land use restriction in line with comparable DHCD programs; and (3) increasing the amount of funding allowed per project from 30% of Total Development Costs (TDC) to 50% of TDC.

State-Aided Public Housing

Initiative: Provide for the capital needs and continued viability of state-aided public housing.

State-aided public housing is a vital resource that serves more low-income households than any other state housing program. It also provides essential low-rent housing supply in an increasingly tight and expensive market. Preserving its viability as the portfolio ages will require careful capital planning and investment. Attending to capital needs will extend the life of the structures and improve the quality of life of its residents. The cost-effective revitalization of public housing can be accomplished by focusing on several key steps.

Planning and Funding Capital Improvements

1. Move toward better local, development-based, long-range capital planning that is essential to the proper asset management of a real estate portfolio. To effectively implement such a system, DHCD will:

   a) Create a more detailed capital improvement planning tool than is currently available—one that considers not just the age and useful life of building components, but also their actual condition based on physical inspection. DHCD is developing a statewide, Internet-based program that will assist housing authorities and DHCD to develop both local and state capital improvement plans. Local housing authorities (LHAs) will be able to begin implementing the new system next year.

   b) Require LHAs periodically to evaluate and report on the condition of all building components and systems, with technical support to ensure accurate evaluations of technical building components. DHCD would assist and audit the inspection process.

   c) Finance and implement a long-term capital plan to address these capital needs. Given the lead times involved in designing and bidding projects, a bond bill including funds for public housing modernization will need to be enacted in 2003 to assure no interruption in the modernization project pipeline when current capital spending authorizations are exhausted.

   d) In the long term, seek to move from periodic selection of modernization projects for funding to providing local housing authorities with predictable, annual capital improvement allowances. DHCD would maintain careful technical and financial oversight and statewide coordination of spending. Housing authorities would be able to plan their capital improvement programs. Placing more responsibility for capital improvement decisions closer to the developments at the local level mirrors the asset management approach effectively employed by the private sector and fosters greater concern for carefully implemented preventative maintenance plans.

   e) In the long term, permit LHAs to establish and provide annual funding for capital replacement reserve accounts. A capital replacement reserve is used to accumulate funds for the replacement of capital items when they become necessary. The annual funding of capital replacement reserves with operating income is a prudent and standard real estate management practice.

2. Use leveraged financing to attract private financing for public housing modernization. Tapping this funding source could provide millions in additional funding each year. (This initiative is discussed in greater detail below.)

Statutory Changes Generating Financial Efficiencies for Public Housing and Local Housing Authorities

Several statutory changes would allow the Commonwealth to maximize the efficient use of its valuable public housing resources. They include:

1. Adopt the Cellucci-Swift Administration's current proposals for the reform of public construction laws. This will save money by encouraging more contractors to compete for smaller public construction jobs, while also speeding up project schedules.

2. Transfer older "empty nesters' (age 55 to 59) who have empty bedrooms in family developments to Chapter 667 elderly housing and free up larger units for other families on waiting lists by authorizing DHCD to convert existing Chapter 667 units for the elderly and disabled to Chapter 705 family units for these tenant households. Permitting such a move would allow the Commonwealth to house a family without expending any funds for the construction of a new unit.

3. Allow DHCD to lower the admission age for certain elderly developments having no waiting list of eligible applicants from 60 to 55, to prevent vacancies in areas with limited demand for elderly housing. This practice, already allowed in federal public housing, would generate income from otherwise vacant units, while providing affordable housing to individuals who need it. (These low-demand areas may disappear in the next decade as the baby boom generation begins to enter its sixties.)

4. Create a 27½% rent structure for tenants who pay their own electric utility costs. Under state law, currently tenants who pay no utility costs pay 30% of their income for rent, while tenants who pay any utility costs pay 25% of their income for rent, regardless of whether they pay for heat and electricity or just electricity. A middle tier rent equal to 27½ % of income would create an equitable rent for those who pay for electricity but not for heat, and it would also realize cash flow that could be used to improve operations, maintenance, and capital planning.

Leveraged Financing for Public Housing

A New Vision for Financing Public Housing

For public housing to become more market driven and less isolated from the larger community, its tenant mix must include tenants with a broader range of incomes. A higher percentage of working families will not only create role models for young residents, bring financial and social resources into the community, and ease the burden of management, but it will also force management to be more responsive because it needs to attract tenants who have more than one housing option. While public housing developments will rarely be attractive to middle or upper income households, there is a market for families with incomes in the 30% to 50% of median range, many of whom face serious housing difficulties.[87] To make developments attractive to such residents, public housing management must have the same incentives as private managers. State public housing developments will also need significant rehabilitation, requiring funds unavailable solely from the state. The ultimate vision is of a community that is an integral part of the surrounding neighborhood, with the vast majority of residents holding jobs and moving toward self-sufficiency.

The Proposal

Last year, a number of housing authorities were awarded multi-million dollar capital grants for substantial improvements, primarily kitchen and bath rehabilitation. An initial screening indicates that the rental market in some of these communities is tight enough to make feasible the targeting of higher income tenants.

In these cases the Commonwealth may be able to apply a simple leveraged financing model which utilizes a combination of tax exempt bonds and a grant of state capital funds of public housing modernization, part of which will pay for direct project costs and part which will provide credit enhancement for some of the bonds. This plan could significantly reduce the amount of state capital funds needed for a project, thereby freeing up those funds to enhance the project or to meet pressing capital needs elsewhere.

Proposed Income Targeting Methodology

The leveraged financing concept depends on targeting a portion of the units in a development to tenants with a broader range of incomes than is typically found in public housing. For example, the income of families in a typical development might be approximately 14% of the area median income. For a family of four in the Greater Boston area this translates into an annual income of approximately $9,170. Since public housing rents are set at 30% of income, this family would pay a rent of about $229 per month. A 100-unit development housing families at this income level would generate about $22,900 in rental income each month.

However, as shown in the chart below, if 60% of the units remain targeted to extremely low-income families averaging 14% of median income, but 20% of the units in this development are targeted to families at 30% of median and another 20% are rented to families at 50% of median, the project's monthly rental income grows to $39,940, an increase of $17,040 each month.

[87] According to Harvard's Joint Center for Housing Studies, more than two thirds of households in the Northeast with incomes below 50% of median pay more than 50% of their income for housing or live in inadequate housing.

Table 7: Monthly Rental Income Generated In A 100-Unit Development With Leveraged Financing

Tenant Income Mix	Number of Units	Percent of Total Units	Average Rent	Percent of Area Median Income	Monthly Rental Income
Current Mix	100	100	$229	14%	$22,900
Leveraged Finance Income Mix	60	60%	$229	14%	$13,740
	20	20%	$491	30%	$9,820
	20	20%	$819	50%	$16,380
Lev.Fin.Total:	100	100%	$399	25%	$39,940
		Increase in Monthly Rental Income:			$17,040

Generally, large urban housing authorities operate at a deficit, subsidized by DHCD for state developments. If, as shown here, rental income increases by $17,040, a deficit authority simply receives a smaller subsidy under the standard formula. However, if DHCD freezes the authority's subsidy at its earlier, higher level, the increase in rental income is fully available to support borrowing to finance capital improvements. This increase in income will repay the loans or bonds and maintain the property without deferring maintenance. This would improve the long-term viability of the development and substantially reduce the current and long-term burden on public housing modernization bond funds.

Restructuring key developments in this manner would also contribute to the long-term viability of the portfolio by making hard to replace developments more welcome in their communities and forestalling pressures to demolish them. Targeting some units to households who are not at the lowest income levels as part of a leveraged financing program would in the short term reduce the number of units available to the lowest-income households. In the long term, however, it would help preserve a far larger number of units. In addition, DHCD has recently applied for and won significant numbers of new Section 8 subsidies and has decided to project-base 100 Section 8 vouchers in a demonstration project to provide some deep-subsidy units in privately owned affordable housing. This project-based Section 8 initiative also partially offsets units that would no longer be available to the lowest-income households as a result of leveraged finance projects.

Leveraged financing could be used in developments that have vacancies that can be targeted to a higher than usual income tier. When used elsewhere, units would be freed up for targeting upon turnover. State law would not permit tenants to be displaced and left without housing.

Proposed Financial and Credit Enhancement Structure

A leveraged finance project would be funded by a combination of debt sized so that it could be supported by project cash flows (rents and a stable state subsidy, as described above) and a traditional capital grant to fill the gap between the supportable debt and project costs. To attract private investors and maximize the amount of debt that can be carried with a given projected rent stream, it would likely be necessary for the Commonwealth to provide a credit enhancement for at least a portion of debt in a leveraged finance project. The Department of Housing and Community Development is designing a credit enhancement mechanism in which the state would initially retain all construction risk (as it does in a conventional modernization project) by standing behind all bonds issued to finance a project until construction is complete and the units rented for two years. Thereafter, the state would continue to stand behind only a small, relatively risky slice of the debt. This would allow the bulk of the debt to be secured only by the property and its cash flows. This latter tier of debt would not require an ongoing guarantee because it would be sized so that ample cash is projected to be available to service it—perhaps 150% as much cash as would be needed to make the bond payments.

A more detailed description of the financing structure is as follows:

1. As noted above, DHCD commits to maintaining the level of operating subsidy received by the project before income targeting is instituted, with annual increases of about two percent, subject to appropriation. (If sufficient operating funds are not appropriated by the legislature, then bonds may be redeemed to reduce debt service, or the income mix may be altered to generate additional rental income.)

2. DHCD makes a modernization grant award for the total development cost (TDC) of the project and executes with the local housing authority (LHA) a contract for financial assistance (CFA) in that amount.

3. DHCD authorizes the LHA to borrow short term for construction/bridge funds, using the anticipated proceeds from the CFA as collateral. The LHA executes a bond anticipation note with the construction/bridge lender for the amount that represents the leveraged financing to be advanced at stabilized occupancy.

4. DHCD authorizes the LHA to borrow long term using the property and the rental income stream as collateral. Construction/bridge financing is retired using the long-term financing once the redeveloped project reaches stabilized occupancy. The remainder of the cost is covered by a traditional capital grant from DHCD.

5. All long-term bonds are secured through the CFA for two to three years after the project is complete and the units have been rented. In this manner, the Commonwealth retains construction risk, as it would in a traditional grant-funded project.

6. When stabilized occupancy has been achieved for two to three years, the senior bonds will be secured by a generous level of debt service coverage (probably 1.5 times debt service), and will no longer be guaranteed by the state through the CFA. The state will continue to stand behind only a small portion of the debt. If necessary at this time, the LHA will use CFA funds to redeem long-term bonds as necessary to reduce the project's debt and achieve the required level of debt service coverage. The remaining CFA funds previously guaranteeing this portion of the debt will then be reallocated to other developments or communities.

7. A second series of junior bonds (the credit enhanced debt) with a lower level of debt service coverage (probably 1.15 times debt service) will continue to be guaranteed by the CFA. If the debt service coverage level drops, then the LHA will again use CFA funds to redeem these junior bonds as necessary to reduce the project's debt and restore the appropriate level of debt service.

Student Housing

Initiative: Promote the development of student housing in Boston and other communities where students place pressure on local housing markets.

Increasing student housing is a win-win proposition for communities and institutions. It decreases pressure on local rental markets while at the same time making universities more attractive to potential applicants. Done correctly, it can also provide a rationale and serve as a process to bring communities and institutions together around a common goal, helping to build the bonds of trust that too many institutions have failed to cultivate with their host neighborhoods.

Recommendation 1: Build on the Davenport Commons model to help ease neighborhood resistance and make financing work.

Three years ago, Northeastern University undertook a project to build a dormitory in South Roxbury that met with local opposition. The story has a happy ending: ground was broken on the Davenport Commons Student Apartments this past fall with strong local support. With the state and city acting as facilitators, the university and community groups were able to unite around a solution that eventually provided something for everyone. The university received the space it needed from the BRA to add 625 dormitory beds. The community received 75 new homeownership units financed with the help of the university, MHFA loans, and equity contributions from the state Department of Housing and Community Development, the City of Boston, and the Federal Home Loan Bank. The city and state were able to relieve some pressure on the tight Boston housing market.

While achieving this solution took three years, the result is an innovative model for developing a combination of student and affordable housing that can be adapted to fit similar situations throughout the Commonwealth. Such situations include any instance where an institution wants to expand its student housing in the face of local opposition. The elements of this model include the following:

- institutional investment in community housing as well as student apartments through a partnership with local community development corporations;
- participation of local and state officials to facilitate agreement with neighborhood groups;
- cross-subsidization of community housing with student housing fees;
- investment in the community tailored to local needs – homeownership units, rental units, retail space, or public space;
- MHFA financing utilizing a 501(c)3 structure to preserve scarce tax-exempt private activity bond volume cap;
- access to state, local, and federal equity housing subsidy programs; and

- private development of student and community housing to minimize costs.

This model has many advantages. It involves local and state officials in the process at the outset to help mediate community concerns. MHFA can provide flexible financing terms to meet the needs of the institutions with regard to items such as amortization and payment schedule, and the use of lease financing avoids the need for issuance of debt by the institution. Finally, access to state and local housing subsidy programs provides an appropriate level of burden sharing for community investments. In essence, the Davenport Commons model provides a forum in which all sides can negotiate a solution. The college or university investment in its own goals is leveraged with funds from other sources to meet community goals as well, giving both sides a victory.

In future iterations, this model could be simplified to streamline the number of subsidies provided to any one deal. At the same time, the state should explore matching non-housing grant programs with these transactions, given particular community needs. For instance, a community that feared the growth of their local college not because of pressure on the housing market but because of a desire to preserve open space might be amenable to a transaction that coupled a dormitory with a new park funded by both university and state open space grant funds. Similarly, grants for transportation or sewers could be matched with university contributions to address needs in those areas.

For institutions that do not want to take on added responsibility for managing new facilities, the model could include a privatized or turnkey option where private developers manage not only construction but also the on-going operation and maintenance of the facilities. Such models are common in many other parts of the country, but have not taken hold in New England. Private student housing operators not only relieve institutions of the trouble of managing facilities, but they also have experience in other settings. This means they can bring new methods or technologies to bear, lowering costs and increasing the potential for community investment.

To send a clear message to the academic community that the Davenport Commons model is viable for other institutions, MHFA and DHCD should strongly encourage these projects. If an institution and locality rise to the challenge and agree to combine student housing with community investment, they will know the state will have the capacity to support them.

Recommendation 2: Work with existing university consortia and umbrella organizations to build joint facilities.

Scarce land and limited capacity to manage residential real estate means that even in a best case scenario relatively few new student housing developments can begin each year. When an opportunity to launch a project exists, multi-university collaboration can maximize its benefits. Smaller institutions could lease floors in developments sponsored by larger institutions, allowing them to house some students without becoming a property manager or taking on the full costs of development. Schools with large numbers of graduate or part-time students, including some of the state's larger colleges and universities, could mitigate the risk of vacancies by banding together. In instances where a community investment will facilitate the development of a project, the burden of the investment can be spread across many institutions.

While these are all powerful reasons for institutions to approach housing in a cooperative manner, several reasons explain the lack of such a strategy until now. A culture of institutional autonomy undercuts a cooperative approach. Furthermore, many institutions view housing as a method for enhancing their unique academic environment.

To enhance cooperation in student housing construction, existing university consortia and umbrella organizations like MassCo., the Fenway Alliance, and others should take the lead in opening discussions about cooperative efforts. Graduate students, such as medical students located at the Longwood Medical Area, may be the most fruitful market segment to target because few schools would demand that graduate housing be imbued with the particular academic environment of an institution or the student services needed in undergraduate dormitories. As noted above, graduate housing may benefit from spreading the risk of vacancies, since such students typically seek out many housing options.

The state should also encourage public colleges and universities to cooperate on housing projects. Through the State College Building Authority, state colleges already consolidate their financing of student housing facilities. Consolidating facilities is a relatively modest next step. There may even be an opportunity to build a multi-institution dormitory on land currently slated for the Massachusetts College of Art project. The project already envisions leasing 60 dormitory beds for the School of the Museum of Fine Arts. Further collaboration could result in an additional 250 beds being built on the site.

Recommendation 3: Encourage universities to review building guidelines to lower costs and take advantage of the newest technologies.

As noted above, colleges and universities may have antiquated guidelines for construction of student housing. These guidelines include rules that dictate standards of construction appropriate for the institutional structure of traditional dormitories but may not be necessary or cost-effective in the context of the increasingly popular apartment style of residence hall.

The academic community should set up a task force to review their guidelines and identify areas in which they can be updated to lower costs or allow for more modern technology. The State College Building Authority should also identify best building practices from Massachusetts and across the nation and circulate these to all Massachusetts colleges and universities.

One reason that Massachusetts may lag behind other states in embracing new building methods is the lack of partnered student housing in the state. Colleges and universities should consider using these methods, not just because they streamline the costs of development and operations, but also because they bring new methods and technologies from other areas into our state. The State College Building Authority and the University of Massachusetts can take the lead in encouraging a market in partnered student housing, as state colleges and universities have in other states, particularly in the Southeast.

Recommendation 4: Create a partnership between universities and MHFA to assist first-time homebuyers of 2-3 family buildings to provide scattered site student/faculty housing and stabilize neighborhoods.

A common complaint neighborhood groups have against colleges and universities is the prevalence of students living in buildings owned by absentee landlords. With the extraordinary wear and tear imposed on the buildings by students and the lack of an on-site owner to provide maintenance, such buildings can too often become run-down, negatively affecting the neighborhood and leading ultimately to the loss of units. By partnering with MHFA to assist first-time homebuyers, colleges and universities can address this issue, assist in providing affordability to moderate-income homebuyers, and provide themselves with versatile housing options for students, faculty and staff. If targeted to specific areas that traditionally have attracted large numbers of students, such a model could achieve off-campus housing that makes a better neighbor without displacing local residents.

Universities and colleges could offer to lease the rental units on a long-term basis in owner-occupied buildings purchased in their neighborhood by MHFA loan recipients. If the lease were to run the term of the mortgage, a rent stream would be assured, and the mortgage loan would be more credit-worthy, perhaps allowing a lower-income buyer to become a homeowner than would otherwise be possible. This would be a benefit to both MHFA and the homeowner purchasing the building. The homeowner would also be relieved of the responsibility of marketing the unit. Finally, if the students housed in the building are unruly, a common complaint in student neighborhoods, the homeowner could have recourse to the university's dean of students. These units would also be ideal for students who do not traditionally reside in dormitories, such as students with families or graduate students.

In areas where additional residence hall development is not feasible, such an arrangement would give universities access to units without having to build new dormitories. By having the students in owner-occupied housing instead of absentee-owned housing, the university would also mitigate the negative effects students may have on neighborhood stability. To the extent there are not sufficient units near university campuses that qualify for MHFA program, MHFA could finance the purchase of units requiring substantial rehabilitation and the university can finance the rehabilitation through a low interest or "soft" second mortgage. While this will require the university to invest its own resources, it will eliminate dilapidated buildings from the neighborhood, ultimately benefiting the institution.

Recommendation 5: Encourage universities to build partnerships with their communities

While this report has identified the lack of land as the critical impediment to new student housing construction, often the lack of land is the result of difficult relations between colleges and universities and their communities. A key to improving such relations is the creation of an ongoing partnership between universities and communities.

Clark University in Worcester has created a prime example of such a partnership. As noted above, Clark University has faced little recent opposition to its growth plans. This is because its extensive community investment plan has created significant local goodwill. Among the elements of this plan are the following:

- establishment of a community development corporation focused on the area surrounding the Clark University Campus;
- the financing by the university of more than 170 residential units in the neighborhood and the renovation and sale of fourteen homeownership properties;
- partnership with neighborhood schools, including the creation of a new grade school with funding from the university and active university involvement by both faculty and students;

- full-scholarships for neighborhood children admitted to the university;
- incentives for faculty and staff to live in the neighborhood through mortgage subsidies and salary bonuses; and
- investment in neighborhood economic development.

This investment in its community has benefited Clark University in many ways. Most significantly, it has led to real improvements in the surrounding neighborhood. The effort has also resulted in improved relations with the community. The participation of Clark in the Worcester public school system is evidence of this, as is the fact that the city has turned over abandoned properties that were in tax default to the Main South CDC supported by the university.

The improved relations between Clark University and the City of Worcester have led in turn to less opposition to the school's expansion plans. Unlike the experience of Harvard University when it purchased land in the Allston neighborhood of Boston, these purchases have aroused no public recriminations.

While Clark University has a unique situation in Worcester, including a neighborhood where housing could be purchased and renovated relatively inexpensively, its commitment can be duplicated elsewhere in the Commonwealth. To assist universities in making this commitment, the state can work with schools to identify opportunities for positive engagement with their communities and highlight positive practices of other institutions. To the extent that universities are willing to invest in their communities, sound projects receiving such investment should score highly in competitive rounds for state funds, allowing university investments to be leveraged with state and federal funds.

Conclusion

Over the last year, the Cellucci-Swift Administration has been examining the causes and effects of the excessively tight housing market in Massachusetts. It is clear that housing affordability is becoming a greater problem as the housing market fails to respond to price increases with the increased production that one would expect. Traditional affordable housing programs help those who have a housing subsidy, but they have not and cannot address the wider problem of affordability caused by production impediments that do not allow market forces to work as they should.

The state continues its commitment to affordable housing through an expansive array of programs. This report points out that more than $1.3 billion per year spent by state and federal agencies to produce, preserve or subsidize housing and that nearly one-quarter of all rental tenancies benefit from some form of subsidy. In addition, a number of programs assist a significant number of first-time homebuyers and low- and moderate-income homeowners.

We must, however, look beyond government programs to long-term solutions. The initiatives outlined in this report shows a way toward real, long-term answers. But the state's housing development problems are not easily solved. They are complex and have been years in the making. Their solution will require an ongoing commitment on the part of those who appreciate the issue's importance to make improvements in the processes that surround housing production. Equally important, the public must more widely be led to understand how critically important it is to remove barriers to housing development so that the housing needs of the Commonwealth's residents can better be served. Bringing down the barriers to change the housing supply dynamics in Massachusetts is essential. The quality of life in our state and our economic future depend on meeting this common, crucial goal.

Appendix A – Executive Order 418

THE COMMONWEALTH OF MASSACHUSETTS

EXECUTIVE DEPARTMENT

STATE HOUSE • Boston 02133

(617) 727-3600

ARGEO PAUL CELLUCCI
GOVERNOR

JANE SWIFT
LIEUTENANT GOVERNOR

BY HIS EXCELLENCY

ARGEO PAUL CELLUCCI
GOVERNOR

EXECUTIVE ORDER NO. 418

ASSISTING COMMUNITIES IN ADDRESSING
THE HOUSING SHORTAGE

WHEREAS, the Commonwealth has enjoyed unprecedented economic growth and prosperity in the last decade;

WHEREAS, as an unfortunate consequence of this economic growth, in many of our communities there is a shortage of housing for individuals and families across a broad range of incomes; and

WHEREAS, to address the housing shortage, we need to encourage our cities and towns to create "community development plans" that identify locations for new housing opportunities while still preserving the unique character of their communities, and to provide incentives to cities and towns to expand the supply of new housing;

NOW, THEREFORE, I, Argeo Paul Cellucci, Governor of the Commonwealth of Massachusetts, by virtue of the authority vested in me as Supreme Executive Magistrate, do hereby order as follows:

The "Community Development Plan" Program

Section 1. The Secretaries of the Executive Office of Environmental Affairs and the Executive Office of Transportation and Construction (the "Secretaries") and the Director of the Department of Housing and Community Development (the "Director"), collectively, shall develop and implement a two-year program to provide technical assistance and resources to cities and towns for the purpose of creating "community development plans." A "community development plan" is a comprehensive, strategic plan for the future development of a city or town, and shall include, among other things, plans for:

- where the community will create new housing opportunities;
- where it will target commercial or industrial economic development (if any);
- how it will improve its transportation infrastructure (or how its existing infrastructure will handle any growth); and
- where and how it will preserve open space.

As part of this program, I hereby direct the Secretaries and the Director, through their respective secretariats and department, to provide assistance to any city or town seeking to create such a plan. Such assistance may include the provision of in-kind services or discretionary funds where appropriate. In no event shall the value of the services and funds provided to any individual city or town for this purpose exceed $30,000. In developing the program, the Secretaries and the Director also shall assist cities and towns seeking to create "regional development plans" that plan for new housing and open space on a regional basis.

The Secretaries and the Director shall develop and implement this program within forty-five days of this Executive Order and shall report to the Governor every three months on its status. Such report shall include which cities and towns have received assistance and their progress in developing their respective plans.

<u>Priority in Distribution of Discretionary Funds</u>

<u>Section 2.</u> The Secretaries and the Director each shall develop and implement a program to give priority in awarding discretionary funds to those cities and towns that the Director of Housing and Community Development has determined are taking steps to increase the supply of housing for individuals and families across a broad range of incomes. Such steps could include:

- adopting revisions to local zoning or land use regulations that provide for more intensive housing development, such as, duplexes, accessory apartments, mixed uses of buildings or sites, or multifamily housing;
- adopting incentive zoning provisions, such as density bonuses for deed-restricted units for low- and moderate-income households;
- streamlining the housing permitting process;
- providing money or land to underwrite the cost of developing housing for low and moderate-income households; and

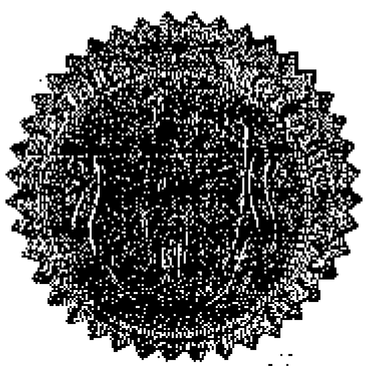
- increasing the supply of housing for low- and moderate-income households by some percentage over existing levels.

As with the community development plans, the programs also should include cities and towns that choose to adopt a regional approach to creating new housing opportunities.

Each program shall be developed and implemented within forty-five days of this Executive Order. The Secretaries and the Director shall provide the Governor with a description of the programs at the expiration of the 45-day period.

Given at the Executive Chamber in
Boston this 21st day of January in the
year two thousand.

Argeo Paul Cellucci
Governor



William Francis Galvin
Secretary of the Commonwealth

GOD SAVE THE COMMONWEALTH OF MASSACHUSETTS

Appendix B - Housing Supply Incentive Program Formula Description

The formula described below seeks to offset the costs that new residential development imposes on cities and towns. Foremost among these costs is education. Therefore, the formula provides cities and towns with the difference between the predicted education costs a new housing unit will impose on a city or town and the revenue the unit will generate in taxes, taking into account additional Chapter 70 Aid a community will receive from higher school enrollment. While education expenses drive the formula, the funds distributed are for any municipal expenses, depending on what the community determines are its needs.

The Formula:

For each $10,000 assessed value cohort, the sum of: (1997-1999 Average Single-family Permits) * (Proportion of 1998 New Homes in each $10,000 Value Cohort) * [(Single-family Coefficient) * (Average Education Expenditure) – (Single-family Coefficient) * (Marginal Chapter 70 Aid) – (Average Tax Rev for a home in each $10,000 value cohort provided the tax revenue is less than predicted education costs net of Chapter 70 Aid)]

Provides the difference between tax revenue generated by new single-family homes and predicted education expenses

+

(1997-1999 Multifamily Permits) * (Proportion of 1998 New Multifamily Units with less than 2 bedrooms) * [(1 BR MF Coefficient) * (Average Education Expenditure) – (1 BR MF Coefficient) * (Marginal Chapter 70) – Tax Rev (Based on Average Multifamily Assessed Value per MF permit issued)]

Rewards production of 1 bedroom or less multifamily units

+

(1997-1999 Multifamily Permits) * (Proportion of 1998 New Multifamily Units with 2 bedrooms or more) * [(2+ BR MF Coefficient) * (Average Education Expenditure) – (2+ BR MF Coefficient) * (Marginal Chapter 70) – Tax Rev (Based on Average Multifamily Assessed Value per MF permit issued)]

Provides the difference between revenue generated by new 2-bedroom or more multifamily units and their predicted education expenses

+

(1997-1999 Average number of Units Rehabilitated) * [(Rehab Coefficient) * (Average Education Expenditure) – (Rehab Coefficient) * (Marginal Chapter 70) – Tax Rev (Based on Average Rehab Assessed Value per Rehab permit issued)]

Rewards rehabilitation of existing units

+

[1-Municipality Adjusted Equalized Valuation Per Capita/(State Average Adjusted Equalized Valuation Per Capita * 150%) * (10% * Original Additional Assistance Amount for those communities below 150% of the State Average Adjusted Equalized Valuation Per Capita)

Returns a portion of the original Additional Assistance funding to poorer communities (those below 150% of the state average adjusted equalized valuation per capita)

Description of Variables:

Variable	Value	Source
1997-1999 Average Number of Permits	City or Town Specific	U.S. Census Bureau
Proportion of 1998 New Homes by $10,000 Value Category	City or Town Specific	Information Request from Municipality
Single-family (SF) Coefficient	0.49	Determined through ANF regression analysis
1 Bedroom Multifamily (1BR MF) Coefficient	0.49	Set at Single-family Level
2 Bedroom Multifamily (2BR MF) Coefficient	1.11 for towns below the 10% Chapter 40B low-income housing threshold, 1.27 for town above the threshold, 3.17 for Boston	Determined through ANF regression analysis
Rehab Coefficient	0.49	Set at Single-family Level
Average Education Expense	Greater of $7,000 (FY 1999 state average actual spending) or FY 1998 Local Foundation Budget	Department of Education
Marginal Chapter 70 Aid	$150	Minimum State Aid
Tax Rev	1.7% (state average residential tax rate) multiplied by the assessed value of the property	Department of Revenue, Information Request from Municipality