Testimony of Granger MacDonald

President, MacDonald Companies

On Behalf of the

National Association of Home Builders

Before the

House Financial Services Committee

Subcommittee on Housing and Insurance

Hearing on

“The Future of Housing in America: Government Regulations and the High Cost of Housing”

March 22, 2016

Introduction

Chairman Luetkemeyer, Ranking Member Cleaver and members of the Subcommittee, I am pleased to appear before you today on behalf of the National Association of Home Builders (NAHB) to share our views regarding regulatory burdens on affordable housing. My name is Granger MacDonald and I am a home builder from Kerrville, Texas and NAHB's 2016 First Vice Chairman of the Board.

NAHB represents over 140,000 members who are involved in building single-family and multifamily housing, remodeling, and other aspects of residential and light commercial construction. NAHB's members construct approximately 80 percent of all new housing in America.

All families deserve a decent, safe and affordable place to call home. NAHB strongly supports sensible policies to facilitate homeownership, increase the supply of quality rental housing and provide rental assistance to low-income households. Today, I would like to discuss how regulations and other barriers impact the affordability and supply of single-family and rental housing.

Cost of Regulation

Regulatory burdens impose costs on the development of land and the construction/remodeling of single-family and multifamily homes. These added costs are passed along to homeowners and renters through higher prices and rents.

Housing is an important source of economic growth and job creation, and regulations are limiting home builders' ability to grow and contribute positively to the economy. NAHB survey data of builders has demonstrated that, on average, regulation imposed during development accounts for 16.4 percent of the price of a home built for sale; regulation imposed during construction accounts for 8.6 percent of the price. Thus, in total, 25 percent of the price of an average single-family home built for sale is attributable to regulation imposed by all units of government at various points along the development/construction process. The regulatory burden includes costs associated with permitting, land development, construction codes, and other financial burdens imposed on the construction process.

As a small business owner operating in a heavily regulated industry, I understand how difficult (and often costly) it can be to comply with the myriad of government regulations that apply to my day-to-day work. This is particularly noteworthy in an industry where margins are so thin and consumers' sensitivity to price fluctuation is so acute.

Oftentimes, these regulations end up pushing the prices of housing beyond the means of many middle-class working American families. For example, according to estimates from NAHB, on a national basis, a $1,000 increase in home prices leads to pricing out just slightly more than 206,000 individuals from a home purchase.[1] Additionally, 110,460 renter households will become burdened by the rising rents if the cost of producing or operating a rental housing unit increases by $1,000. The size of this impact varies widely across states and metro areas, depending on population, income distributions and new home prices. This highlights the real effect that building regulations have on housing affordability.

[1] http://www.nahb.org/generic.aspx?genericContentID=161065&channelID=311

Unintended Consequences of Regulations and Housing Affordability

By reducing unnecessary regulatory burdens on the nation's small businesses, we can promote job creation and reduce costs for consumers. For example, a study by the U.S. Small Business Administration found that firms with 20 or fewer employees pay 40 percent more in compliance costs per employee than firms with more than 500 workers. Smaller firms are typically forced to pay huge added costs to hire outside professional consultants to help them demonstrate compliance with technical and permitting requirements.

Home builders and their subcontractors are among the small businesses that are disproportionately burdened by complicated regulations and expensive compliance costs. Most homebuilding companies are small businesses that employ less than 10 workers and build less than 10 homes annually. These are the types of businesses most urgently in need of regulatory relief.

The overregulation of the housing industry is felt at every phase of the building process. It results from local, state and federal mandates. It includes the cost of applying for zoning and subdivision approval; environmental mitigation; and permit, hook-up, impact or other government fees paid by the builder.

Even now, the homebuilding industry is besieged with regulation that will have negative effects on affordability. NAHB is actively opposing regulations proposed by the Occupational Safety and Health Administration (OSHA), the Environmental Protection Agency (EPA), the Federal Emergency Management Agency and other agencies on new regulations which could drive up the cost of housing further. Specifically, regulations on energy codes, EPA's Waters of the U.S. regulation, OSHA's Crystalline Silica regulation, the U.S. Department of Labor's (DOL) Persuader rule and new joint employer standard, and the Americans with Disabilities Act compliance are only a few of the myriad of regulatory issues home builders must face on a daily basis.

All of these devastating regulations must be factored into the cost of housing. As the cost of housing increases and the access to credit remains tight, home buyers and renters will have fewer safe, decent and affordable housing options.

Homeownership Is Still the American Dream, but Quality Rental Options Are Also In Demand

Younger Americans still look to homeownership as an important part of the American Dream. According to a recent survey from the Demand Institute, of the 1,000 Millennials surveyed, 75 percent believe homeownership is an important long-term goal and 73 percent believe homeownership is an excellent investment. However, 44 percent think it will be difficult to qualify for a mortgage.[2] In 2014, Fannie Mae conducted a survey that found "90 percent of young renters were likely to buy a home at some point in the future. Only 7 percent of younger renters reported that they were likely to always rent a home." This is due to the ongoing preference for homeownership and the "belief that owning a home [is] the sensible long-run financial choice, protecting against rent increases as well as yielding financial benefits."[3] And while a majority of renters in a recent Freddie Mac survey indicated they planned to continue to rent over the short-

[2] http://eyeonhousing.org/2014/09/millennials-and-the-american-dream/

[3] http://www.fanniemae.com/resources/file/research/housingsurvey/pdf/nhsmay2014presentation.pdf

run (the next three years), this share has fallen to 55 percent compared to 61 percent from an August 2014 survey. Moreover, the Freddie Mac survey also revealed that saving for homeownership was an important goal of renters, with 60 percent of respondents placing a high or medium priority on the goal of saving for a down payment.[4]

NAHB believes it is important to focus not only on the affordability of renting, but also look towards the future home owners and ensure that they have the tools they need to move into homeownership.

While most families still aspire to buy a home of their own, this dream is more difficult to achieve today than in the past. Most newly formed households are just beginning their careers and do not have large down payments or high credit scores. Restrictive underwriting standards have placed mortgages even further out of reach for such families. Student debt responsibilities and lower starting salaries and wages compound the challenges facing younger individuals making it even more difficult for them to transition to homeownership without access to affordable opportunities.

In addition to normal underlying housing demand, NAHB estimates that two million households did not form during the recession, and they represent additional pent up demand that will come to the housing market as the economy improves and hiring returns to more normal levels. Many of these individuals either did not form an independent household or they returned to live with their parents, relatives or friends after losing their job or experiencing a significant reduction in income. NAHB expects these individuals to be in the market to rent an apartment or buy a home as the economy expands.[5]

In the multifamily housing business, affordability is a serious problem for families hoping to rent a quality apartment. NAHB's research shows that rents are rising faster than the rate of inflation and wage growth. Similarly, the Harvard Joint Center for Housing Studies estimates that 26.5 percent of rental households in 2013 were classified as rent burdened, paying more than 30 percent of their household income in rent. Additional supply is the solution to rising demand for rental housing.

Economic Impact of Single Family and Multifamily Construction

Homebuilding is American manufacturing. The jobs it creates cannot be shipped overseas. Reigniting and supporting homebuilding directly correlates to additional American manufacturing jobs at all levels.

In the third quarter of 2015, housing's share of gross domestic product (GDP) was 15.3 percent, with homebuilding yielding 3.3 percentage points of that total. Historically, residential investment has averaged roughly 5 percent of GDP while housing services have averaged between 12 percent and 13 percent, for a combined 17 percent to 18 percent of GDP. While these shares tend to vary over the business cycle, clearly housing is an important factor in a healthy economy.[6]

[4] http://www.freddiemac.com/multifamily/pdf/Consumer_Omnibus_Results_Jan_Feb_2016.pdf
[5] http://eyeonhousing.org/2016/02/young-adult-households-that-did-not-form/
[6] http://eyeonhousing.org/2015/12/housing-share-of-gdp-third-quarter-2015/

The homebuilding industry creates a significant number of jobs and added tax revenue. NAHB's national estimates for 2014[7] include the following:

- Building an average single-family home: 2.97 jobs, $110,957 in taxes
- Building an average rental apartment: 1.13 jobs, $42,383 in taxes
- $100,000 spent on remodeling: 0.89 jobs, $29,779 in taxes

The impacts on employment are broad based, creating jobs in many important U.S. industries, such as manufacturing, wholesale and retail trade and professional services, in addition to construction.

Home construction has experienced a slow but consistent recovery since the end of the Great Recession. In 2009, during industry lows, total housing starts came in at 554,000. Of that total, 445,000 were single-family, while 109,000 were multifamily. Since then, the multifamily sector has had the more accelerated recovery. For 2015, total multifamily starts came in at 397,000, a 362 percent gain over the cycle low. NAHB expects multifamily production to be essentially level with a total of 396,000 multifamily starts for 2016. However, rising rents and lackluster income growth have increased rental housing burdens.

Impact of Executive Order 13690 on Housing Affordability

NAHB has serious concerns regarding decreased housing affordability that will result along the nation's rivers and coasts once the Department of Housing and Urban Development (HUD) begins to implement Executive Order 13690 and the new Federal Flood Risk Management Standard (FFRMS).

The FFRMS expands floodplain management requirements, including floodplain avoidance, mitigation, and increased elevation and resilience standards, far beyond the long-established 100-year floodplain limits for all federally-funded projects. While protecting federal investments and taxpayer dollars makes sense, HUD has indicated it will also apply the new flood risk management standard to multifamily projects using FHA-backed loans for new construction and substantial rehabilitation, including its market-rate Section 221(d)(4) program.

Regrettably, HUD has not mapped the geographic limits of the expanded floodplains or analyzed the costs and benefits of implementing the new standard. Without maps of the regulatory floodplain, builders and developers using this financing will face unnecessary uncertainty as they plan multifamily projects. If a project triggers the expanded flood risk management requirements, project delays and costs will undoubtedly increase. In fact, preliminary estimates suggest compliance with the new FFRMS will increase construction costs for new HUD-financed or assisted properties by approximately 5 percent. This estimate is based on the cost of elevating the properties 2 feet above the base flood elevation (BFE). Considering NAHB estimates that the average profit margin on multifamily properties is only about 2 percent,[8] it is clear that delays and increased construction costs pose a serious threat to housing affordability in communities anywhere near the water.

---

[7] http://eyeonhousing.org/2014/05/jobs-created-in-the-u-s-when-a-home-is-built/ and "Impact of Home Building And Remodeling On The U.S. Economy" by Paul Emrath, Ph.D., May 1, 2014 http://www.nahbclassic.org/generic.aspx?sectionID=734&genericContentID=227858&channelID=311&_ga=1.164712319.1923655094.1427310833.

[8] "Homebuilder and Remodeler Cost Breakdown" by Natalia Siniavskaia, NAHB Eye on Housing Blog; January 7, 2016. See http://eyeonhousing.org/2016/01/homebuilding-costs/?_ga=1.7542962.1073388023.1458141654.

Freeboard Value Approach

While E.O. 13690 provides multiple compliance options, HUD indicated (Fall 2015 Unified Agenda[9]) that it will use the freeboard value approach, stating "new construction or substantial improvement in a floodplain [must] be elevated or flood proofed two feet above the base flood elevation for non-critical actions and three feet above the base flood elevation for critical action."

NAHB is gravely concerned that this approach would significantly expand the floodplain area beyond the existing 100-year floodplain. This is because the freeboard value approach is not simply a vertical expansion of the floodplain; it will expand the floodplain horizontally as the elevation rises. **Figure 1** illustrates the floodplain expansion associated with the freeboard value approach. Areas in the gray region are within the 100-year floodplain and are currently subject to the various floodplain requirements. The increased flood elevation is represented by the vertical increase beyond the 100-year BFE, and the horizontal increase (tan region), which expands depending on the topography. These new areas would be subject to the floodplain management requirements.

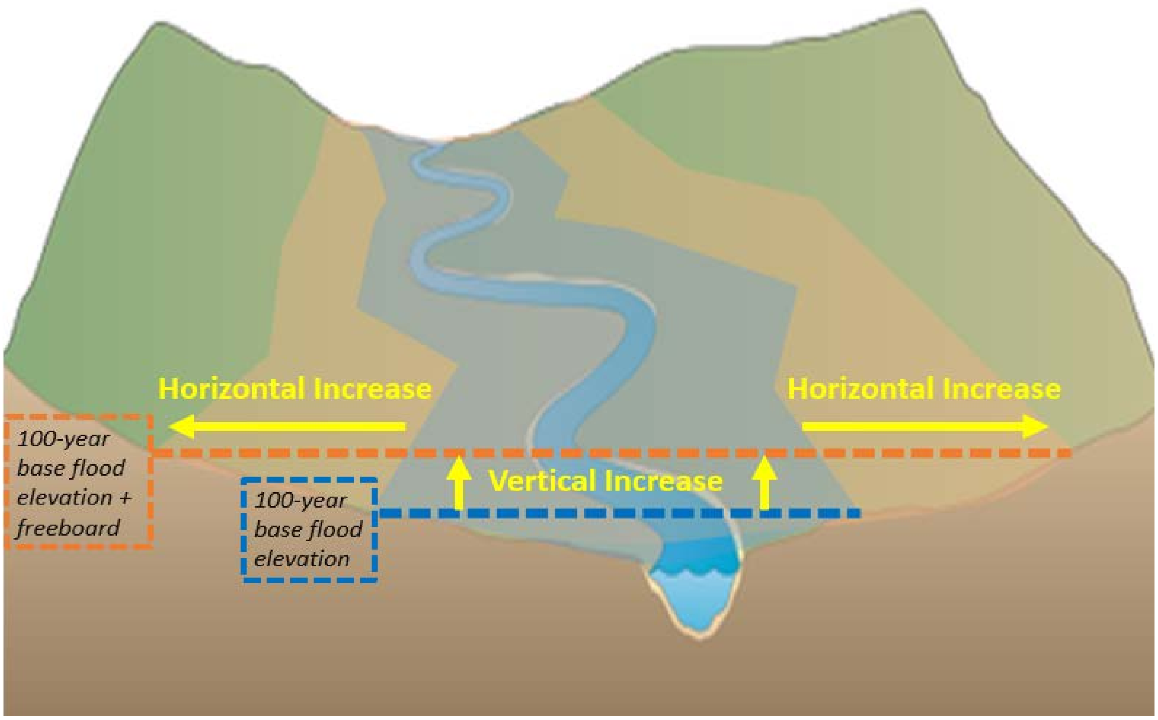

Figure 1. Illustration of the vertical flood elevation increase and corresponding horizontal floodplain expansion under the freeboard value approach. Shaded gray = 100-year floodplain. Shaded tan = freeboard value floodplain.

Unlike the 100-year floodplain, which is mapped by FEMA, there are no national maps to show the floodplain according to the freeboard value approach. Such maps are needed to determine

[9] The Unified Agenda of Federal Regulatory and Deregulatory Actions, more commonly known as the Unified Agenda, is a semiannual publication of all the regulatory actions federal agencies are considering. Executive Order 12866, Regulatory Planning and Review, requires agencies prepare such an agenda in order to improve coordination among divisions of the federal government and to notify the public of upcoming actions.

the extent of the floodplain expansion as well as to help determine a project's feasibility in the newly defined floodplain before builders invest years of their time and potentially millions of dollars securing the necessary financing, land, permits and construction materials. Until such maps are developed, builders may have to rely on surveyors to determine the floodplain boundaries, and it is not guaranteed that HUD officials will agree with these analyses. Due to the uncertainty, additional regulatory burden and increased costs that builders will have to bear under this approach, NAHB has strongly urged HUD not to implement E.O. 13690 via rulemaking until maps defining the new floodplains are produced by the appropriate federal agency.

In the last five years, HUD has financed over 800 projects nationwide using the FHA 221(d)(4) multifamily mortgage insurance program. NAHB is concerned that the cost of the expanded floodplain management standard will be significant and impair the ability to provide affordable housing using numerous federal programs.

Access to Credit

The ability of the homebuilding industry to address affordable housing needs and contribute significantly to the nation's economic growth is dependent on an efficiently operating housing finance system that provides adequate and reliable credit to home buyers and home builders at reasonable interest rates through all business conditions. At present, home buyers and builders continue to confront challenging credit conditions weighed down by an overzealous regulatory response to the Great Recession. In addition, the ongoing uncertainty over the future structure of the housing finance system has intensified these challenges.

The housing finance system is governed by statutes and regulation overseen by a myriad of federal agencies. In response to the recent financial crisis, the Dodd-Frank *Wall Street Reform and Consumer Protection Act of 2010 (*Dodd-Frank) mandated significant mortgage finance reforms and created the Consumer Financial Protection Bureau (CFPB) to supervise and monitor many of the new requirements. Additionally, the Federal Housing Finance Agency (FHFA), the Federal Housing Administration (FHA) and the federal banking regulators all have taken steps to ensure the U.S. economy will never again be as vulnerable to risky mortgage lending. The collective force of the actions taken by these agencies, along with the lingering doubts and uncertainty of market participants, has resulted in an undue restriction on the availability of mortgage credit to many creditworthy borrowers.

While there have been some actions taken by the individual agencies to mitigate the overly tight lending conditions, the housing sector is still struggling to return to normal. NAHB believes there are additional steps that can be taken to eliminate some of the barriers to credit availability and support a stronger, more robust recovery of the housing and mortgage markets while still employing balanced reforms to protect the housing market from another crisis.

Affirmatively Furthering Fair Housing

The Affirmatively Furthering Fair Housing (AFFH) regulation, which HUD is currently implementing, could pose further challenges to producing and preserving affordable housing. NAHB supports the rule's goals of reducing concentrations of poverty and housing segregation as well as providing greater economic opportunity to all residents in a community. However, NAHB is concerned that this initiative could result in unintended consequences with the federal government dictating prescriptions for land use and program design that would be more effective if developed and vetted at the local level. Also, because HUD has authority to withhold housing funds from areas that do not submit accepted fair housing plans, the AFFH rule may also pressure local jurisdictions to undertake misguided and shortsighted quick fixes in order to ensure that federal grants and subsidies are not disrupted, rather than pursuing solutions that are sustainable over the longer run.

Labor Shortages

The homebuilding industry is experiencing a major labor shortage. In 2015, the labor shortage was the number one problem facing NAHB members. As of mid-2015, 41 percent of builders were reporting a shortage of labor in 9 key trades, up sharply from 20 percent in 2012 and 28 percent in 2013. Moreover, in January, we saw an all-time high in unfilled positions since 2007, with 185,000 job openings nationwide in the construction field.[10]

Builders are also concerned about the availability of subcontractors. Over half of our builders subcontract out at least 75 percent of the construction work. Partly as a result, costs of subcontractors are rising faster for builders than costs of directly-employed workers.

Roughly three out of five builders said that labor scarcity has made it difficult to complete projects on time. Labor shortages have caused builders to pay higher wages/subcontractor bids, and raise home prices.

However, the construction industry has an aging population. Data from the 2013 American Community Survey (ACS) reveals that the median age of a worker in the overall construction sector is 42, with some subcontractor median ages ranging in the 50s.[11] There's tremendous financial opportunity in the construction trades, and for those not inclined to the college track, we should be working to encourage careers in construction.

I have experienced the problems that labor shortages have on our industry. Multifamily construction projects that normally take 14 months now take 18 months. Previously, the average cost of multifamily construction in my town was $100,000 per unit, but due to labor shortages it is now $115,000 a unit. With that increase, my business is unable to cover the cost, and it must be passed on to the consumer in the form of higher rent.

It is a common misconception while talking about Davis-Bacon to cite the construction industry as a low paying sector. Trades in residential building and remodeling are good, family-supporting jobs. Carpenters, for example, earn an average of $45,590 per year,[12] while electricians average $54,520[13] and plumbers average $54,620.[14]

Davis-Bacon

The Davis-Bacon Act, created in 1931, is derived from the Depression-era practice of employing workers from lower-paid areas to bypass local workers that required a higher wage. Congress has extended the use of Davis-Bacon beyond directly funded federal projects, such as provisions within the Housing and Community Development Act of 1974.

---

[10] http://eyeonhousing.org/2016/03/elevated-count-of-unfilled-construction-jobs-in-january/

[11] http://eyeonhousing.org/2015/12/age-of-the-construction-labor-force/?_ga=1.174098274.1923655094.1427310833

[12] http://www.bls.gov/oes/current/oes472031.htm

[13] http://www.bls.gov/oes/current/oes472111.htm

[14] http://www.bls.gov/oes/current/oes472152.htm

The law's original intent, however, has been frustrated by burdensome regulations and prevents taxpayers from benefitting from competitive bidding. For NAHB members, the requirement to use Davis-Bacon wage rates can substantially increase the cost of constructing affordable housing. As this law is currently enforced, it is artificially driving up construction costs on apartment communities that include HUD financing. Further, the compliance burdens are creating barriers to entry for small mom-and-pop subcontractors to work on these projects.

The current wage survey process utilized by the DOL often sets the highest industry wages or organized labor wages in an area as the prevailing wage for federal projects. As an industry that is typically non-unionized, many of our home builders and remodelers have little or no experience dealing with the requirements of Davis-Bacon, and the inclusion of its provisions have the tendency to simply discourage NAHB members from participating in federal programs.

Over the years my business has lost many subcontractors due to constraints over Davis-Bacon, including subcontractors we have worked with for over a decade. These smaller subcontractors, like our builder members, are ill-equipped to deal with the compliance burdens and reporting mandates. For example, Davis-Bacon requires the subcontractors, as well as the general contractors, to manage payrolls, make payments and report wage information on a *weekly* basis.

As HUD moves away from paper to electronic reporting of wage and payroll certifications, the new reporting requirements for subcontractors have made it impossible for them to participate in projects that require Davis-Bacon, and as a result, crippled their businesses. The larger companies are able to withstand the requirements, but in my experience, these compliance burdens are disproportionately affecting minorities and mom-and-pop subcontractors. Smaller subcontractors who cannot afford to hire Davis-Bacon compliance staff or consultants do not understand the reporting requirements, do not have the staff or business infrastructure to comply with the mandates, or simply choose to take other jobs to avoid the additional compliance burdens.

The onerous Davis-Bacon requirements are reducing the supply of subcontractors. NAHB estimates that subcontractors account for 65 percent of multifamily construction costs, but it is not only the paperwork burdens that are scaring some builders and subcontractors away from HUD projects where Davis-Bacon applies. Fines and liability associated with Davis-Bacon are a deterrent. NAHB has heard from builders who are held liable for violations of their subcontractors even though the subcontractor submitted certified payroll documentation. In fact, the DOL has held builders accountable for their subcontractor's fraud, such as falsifying certified payroll documents.

NAHB believes that including Davis-Bacon mandates on federal construction projects -- particularly affordable housing construction -- negatively impacts the goals of government programs by unnecessarily creating additional layers of bureaucracy and costs. NAHB strongly opposes the mandatory use of Davis-Bacon prevailing wage rates and requirements.

Inclusionary Zoning

NAHB is concerned that there is too much focus on Inclusionary Zoning (IZ) as the single preferred method of achieving fair housing goals. IZ requires that a portion of new construction is designated as affordable housing for those of low to moderate income.

The reality is that different market segments may require different tools for improving affordability, from direct or indirect subsidies at the low end of the income bracket to better planning for housing and regulatory barrier removal strategies at the upper end of the income range. An economic study conducted for NAHB that focused on price and production effects concluded that in places like California, there was not an overall increase of housing production from IZ and that IZ acts like a tax on housing.[15]

The middle class gets squeezed out under IZ. Due to an increase in the cost to cover subsidized IZ units, the middle class is no longer able to afford the market-priced units and they are ineligible for the subsidized rates. IZ simply shifts the problem without solving it.

IZ may be feasible if the right incentives are available. There are other approaches such as planning and zoning changes to assess development capacity and encourage affordable housing. Expedited permitting processes and advocacy efforts to reduce NIMBYism can also have broad effects on housing affordability.

NAHB urges government to encourage and coordinate with, and not prescribe to, local communities to adopt long-term comprehensive plans that will meet the demand for new housing and economic development. Eliminating exclusionary planning and zoning practices will encourage the production of the full range of housing options for all members of the community.

Coordination and Streamlining of Local Regulations

NAHB also believes that streamlining local regulations and removing unnecessary red tape that delays or prevents development is sorely needed. We wholeheartedly support the Administration's encouragement to local policymakers that they reduce local barriers to housing development. One White House Fact Sheet[16] said:

> "In many productive regions – where companies are flocking to do business – it's harder for them to find workers because it's so hard for those workers to find housing. In some cases, this difficulty is not for lack of developers who are willing to invest, or construction workers wanting to get back to work – it's because localities have not gotten around to reforming outdated, decades-old rules on housing development. Overly burdensome barriers to developing new housing reduce the ability of housing supply to respond to demand, and cause higher housing costs for working families. In the most heavily regulated communities, delays for development approval average ten and a half months, compared to just over three months in less regulated communities…"

Conclusion

Regulatory reforms will help improve affordability, but it is not a substitute for a direct subsidy. A 2011 Harvard study noted that "[t]he rising costs of construction make it difficult to build new housing for lower-income households without a subsidy."[17] In 2009, the median asking rent for

[15] https://www.nahb.org/~/media/Sites/NAHB/SupportingFiles/4
/FIN/FinalResourceManualPublicVersion_20110614041425.ashx?la=en
[16] https://www.whitehouse.gov/the-press-office/2013/08/05/fact-sheet-better-bargain-middle-class-housing
[17] "America's Rental Housing: Meeting Challenges, Building on Opportunities" Joint Center for Housing Studies of Harvard University, 2011. Page 23.

new unfurnished apartments was $1,067; for minimum-wage workers, an affordable monthly rent using the 30-percent-of-income standard is just $377.[18] The study calculated that to develop new apartments with rents affordable to households with incomes equivalent to the full-time minimum wage, the construction costs would have to be 28 percent of the current average.[19] While regulatory reform will help us lower development costs, to reach lower-income households, it is financially infeasible to construct new, unsubsidized affordable rental units without federal assistance.

As we urge Congress to pursue regulatory reform, we also request your continued support for successful housing programs such as the Low Income Housing Tax Credit (LIHTC), and full funding for vital rental housing programs such as the Housing Choice Voucher Program, Project-Based Section 8, and HOME.

Additionally, streamlining the regulatory process encourages the promotion of new development. NAHB applauds the Committee for their work on H.R. 3700, the *Housing Opportunity Through Modernization Act of 2016,* which reduced the inefficient and duplicative requirements that have made many of the HUD and Rural Housing programs unnecessarily burdensome.

NAHB thanks the Subcommittee for the opportunity to testify. Whether they rent or own, Americans want to choose where they live and the type of home that best meets their needs. NAHB thanks the Chairman and this Subcommittee for their leadership on this important issue, and stands ready to work with you to achieve necessary reforms and expand the availability of affordable housing.

---

http://www.jchs.harvard.edu/publications/rental/rh11_americas_rental_housing/AmericasRentalHousing-2011.pdf

[18] Page 23 and 21

[19] Page 24