February 20th, 2024

Testimony for House Bill HB0538:

Land Use – Affordable Housing – Zoning Density and Permitting (Housing Expansion and Affordability Act of 2024)

Position: Neutral (Informational Only)

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Summary:

Within a 1-mile radius of rail stations, upzoning to 4 units per lot in areas currently zoned for single-family detached (SFD) homes presents the following opportunities:

- A total of 93,000 homes, at 4 units per lot, would be economically viable for Middle Housing conversion.

- We project that roughly 5,100 additional units would be built each year for the next 30-40 years.

  - With an inclusionary zoning (IZ) requirement of 1 unit being set aside for a household earning 60% or less of area median income (AMI), we project this number would drop to around 1,000 units – or by around 80%.

  - Building more housing would also jumpstart the filtering process, where older homes are passed down to lower-income households.

- The price of the newly built Middle Housing units would be around $400,000 after conversion, roughly half of the value of SFD homes built from 2010-2022 in the same areas and about 78% of the value of the SFD homes they replaced. (Detailed price distribution below.)

  - The projected price distribution of new Middle Housing units would be entirely within the price range of homes actually bought by low-income households in 2022.

Other considerations:

- If applied across the state, and not just around rail stops, the supply effect could be as large as 19,000 additional units (at a density of 4 units per parcel) and 29,000 additional units (at a density of 8 units per parcel). (Detailed results below.)

- A strategy that focuses exclusively on multifamily (either by leaving in place single-family zones or imposing IZ mandates on Middle Housing) may have the unintended consequences of creating islands of density. These islands will have lots of people and amenities, which will drive up land values, including for surrounding areas.

  - The single-family homes in these areas will over time be converted to McMansions (large opulent homes) that will remove a relatively affordable older unit from the supply and replace it with an expensive unit.

Map of 1-mile buffer around Maryland railway stations
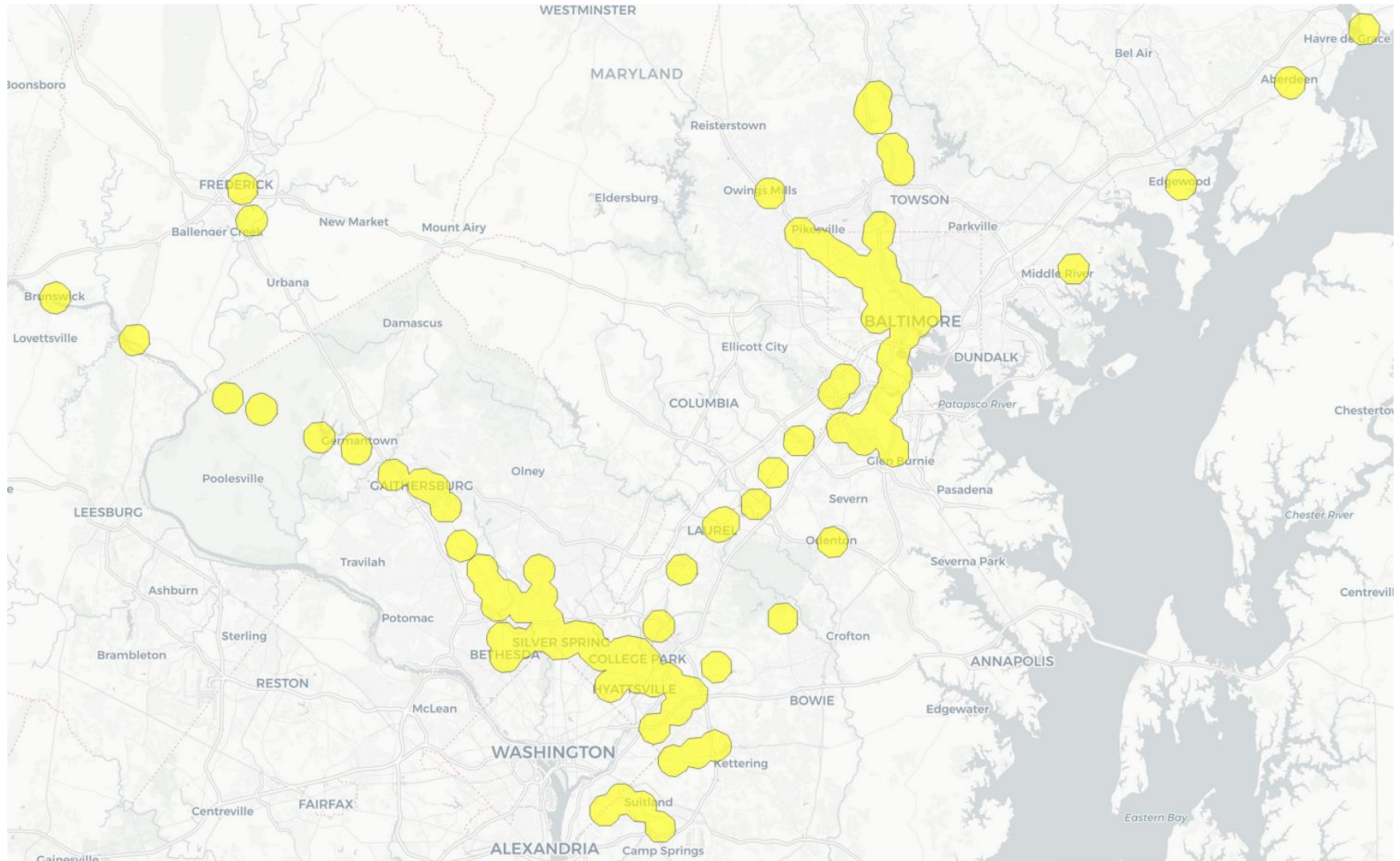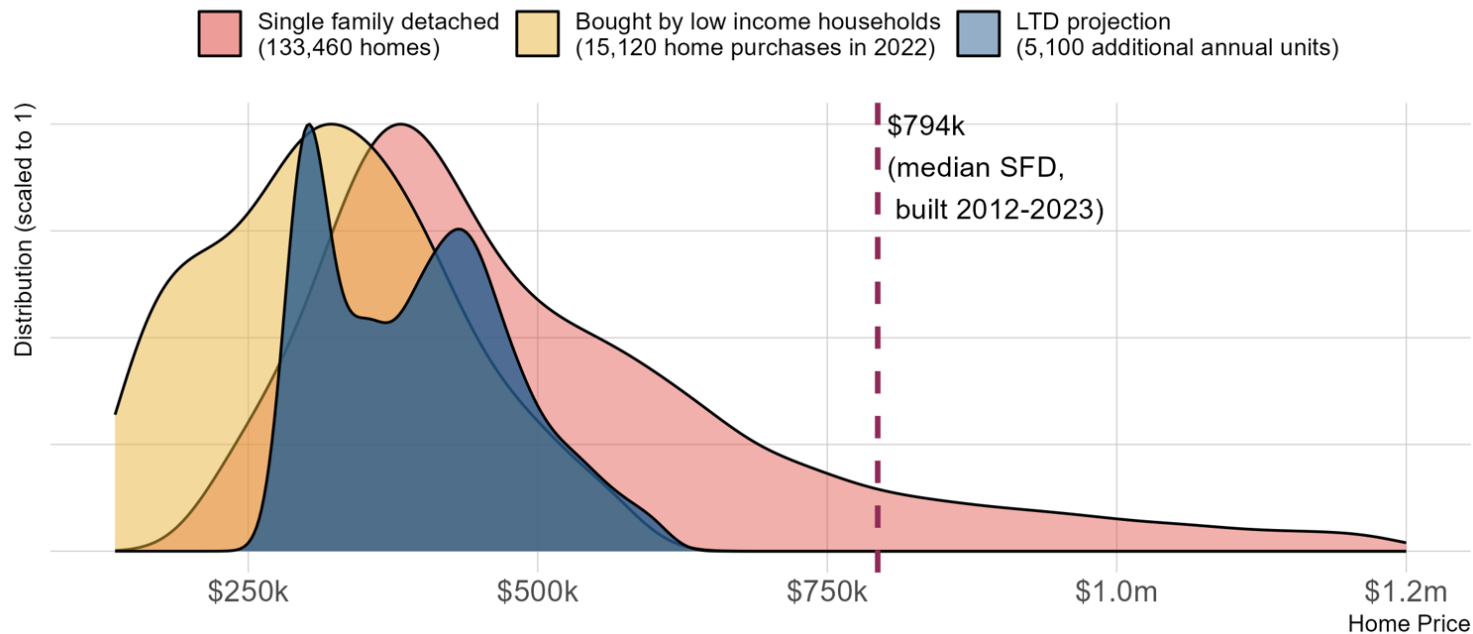

Source: Transit Explorer and AEI Housing Center.

Estimated Price Distribution of New Middle Housing – around 1-mile buffer of Maryland railway stations

The below chart shows the home value distributions (using an Automated Valuation Model from Dec. 2022) of the outstanding single-family detached housing stock around a 1-mile buffer of Maryland railway stations and our projections for the townhome conversion price points. We also overlay the price points at which low-income borrowers (those with < 60% of AMI) purchases homes in 2022 (per HMDA data).

All Middle Housing conversions would be within reach of low-income borrowers, while new SFD housing built between 2012-2023 are much higher valued and hence further out of reach.

Boosting naturally affordable housing near Maryland transit

Light-Touch Density would would reduce housing pressure by creating **5,100 additional homes annually** affordable to **low income households**

Legend:
- Single family detached (133,460 homes)
- Bought by low income households (15,120 home purchases in 2022)
- LTD projection (5,100 additional annual units)

$794k (median SFD, built 2012-2023)

Y-axis: Distribution (scaled to 1)
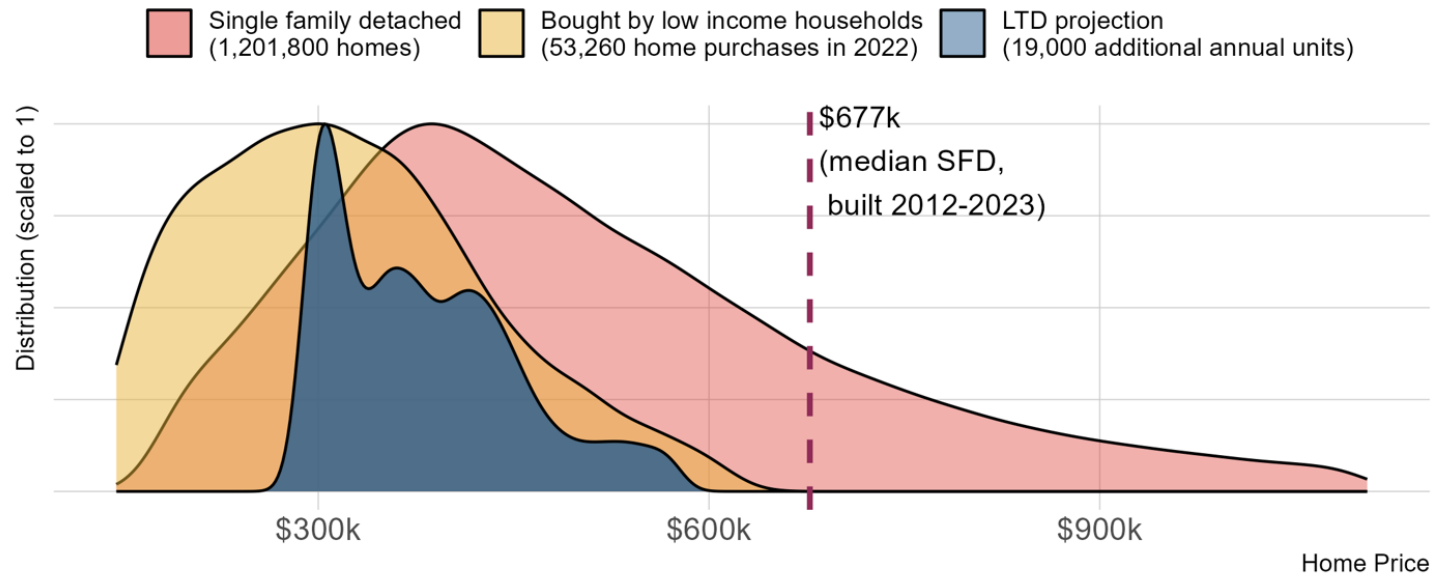
X-axis: Home Price — $250k, $500k, $750k, $1.0m, $1.2m

Restricted to 1-mile buffer around rail stations, SFD/LTD by property location, purchases by intersectng tract boundary.
Source: AEI Housing Center, HMDA, Public Records. Trimming the top and bottom 5% of each distribution.
Low income households earned less than 60% of county median income in 2022.
LTD projections based on a max of four units per existing SFD lot. More information at heat.aeihousingcenter.org.

Estimated Price Distribution of New Middle Housing – all of Maryland

Same chart as above but with different geography.

Boosting home production affordable to Maryland's low income homebuyers

Light-Touch Density would would reduce housing pressure by creating **19,000 additional homes annually** affordable to **low income households**

Legend:
- Single family detached (1,201,800 homes)
- Bought by low income households (53,260 home purchases in 2022)
- LTD projection (19,000 additional annual units)

$677k (median SFD, built 2012-2023)

Y-axis: Distribution (scaled to 1)
X-axis: Home Price — $300k, $600k, $900k

Source: AEI Housing Center, HMDA, Public Records. Trimming the top and bottom 5% of each distribution. Low income households earned less than 60% of county median income in 2022. LTD projections based on a max of four units per existing SFD lot. More information at heat.aeihousingcenter.org.

Detailed Modeling results:

Note that we model different scenarios based on the areas the policy would apply and the maximum allowable density.

LTD refers to Light-touch Density and is equivalent to Middle Housing in the context of this analysis. Most of the new units will be townhomes.

The results are for 1 year and we would assume that they would continue for the next 30-40 years assuming a market need for more housing.

These estimates are based on a variety of case studies that allowed some sort of Middle Housing in the past.[1] Since these legal changes were made decades ago, they allow us to evaluate the outcomes. In these case studies, we found that each year about 2% of parcels were converted to a higher and better use. For every parcel in Maryland, we estimate its economic viability to be converted to a higher and better use. We then assume that 2% of properties, for which the economics work, are converted each year. We also estimate the price point of the new Middle Housing types and plot the potential additional units on a map (see appendix 4).

For the detailed methodology, see here: https://www.aei.org/wp-content/uploads/2023/06/State-and-Local-Upzoning-Bill-Infill-Conversion-Estimates-Methodology-v6.pdf

To model the numbers with an inclusionary zoning (IZ) mandate, we orient ourselves on Seattle's experience, which implemented an IZ requirement in 2019. As a result, townhome permits dropped 80% over the next years. For more on this, see appendix 2.

Maximum density (units per lot)	Cumulative net additional LTD conversion units after 1 year*			
	All State		Properties within 1 mile of a rail station	
	no IZ	with IZ	no IZ	with IZ
4	19,090	3,818	5,120	1,024
6	26,431	5,286	7,071	1,414
8	28,790	5,758	7,627	1,525

* Assumes that an IZ mandate reduces the economic viability by 80%.

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[1] Palisades Park, NJ: 1939 zoning law allowed 1- or 2-units on any parcel. Charlotte, NC: R-MF zoning allowed small scale residential structures to be built in less than 5% of Charlotte's neighborhoods. Houston, TX: In 1998, the minimum lot size requirement decreased from 5,000 square feet to effectively 1,400 square feet within the city's I-610 Inner Loop. Seattle, WA: In the mid-1990s, the creation of the Low Rise Multifamily (LRM) zone allowed property owners to use their land more efficiently leading to a townhome construction boom. Tokyo, Japan.

Maximum density (units per lot)	Cumulative net additional LTD conversion after 1 year as a % of 2017-2021 5-year ACS total housing units*			
	All State		Properties within 1 mile of rail station	
	no IZ	with IZ	no IZ	with IZ
4	0.8%	0.2%	0.2%	0.0%
6	1.2%	0.2%	0.3%	0.1%
8	1.3%	0.3%	0.3%	0.1%

* Assumes that an IZ mandate reduces the economic viability by 80%.

Maximum density (units per lot)	Median est. per unit price after LTD conversions relative to a buyer's AMI*	
	All State	Properties within 1 mile of a rail station
4	97%	98%
6	84%	83%
8	76%	76%

* We arrive at the prospective buyer's income as a share of AMI by multiplying the estimated price point by 3, which is a "normal" price-to-income ratio.

Maximum density (units per lot)	Median est. per unit price of LTD conversions as a % of original unit	
	All State	Properties within 1 mile of a rail station
4	78%	78%
6	63%	64%
8	53%	54%

Maximum density (units per lot)	Cumulative net additional homeowners after 1 year*			
	All State		Properties within 1 mile of a rail station	
	no IZ	with IZ	no IZ	with IZ
4	15,272	1,527	4,096	410
6	21,145	2,114	5,657	566

| 8 | 23,032 | 2,303 | 6,101 | 610 |

* Assumes that 80% of Middle Housing units will be owner-occupied, similar to the current percentage. For more, see appendix 3.

Source: AEI Housing Center.

Appendix 1: McMansion conversion example in Bethesda

Consider a McMansion in Bethesda, which has more teardown McMansions than any other place in Maryland. To illustrate why McMansions get built, we look at a case study of two homes in the same Census block – one which has been redeveloped, and a prospective home on a same-size lot that has an economic case for either LTD or McMansion development.

Note that the McMansion conversion rate is about 1.6% of economically viable parcels per year, not too different to the 2% conversion rate for Middle Housing.

Image source: Google.
Address of top image: 7205 Honeywell Ln, Bethesda, MD 20814
Address of bottom image: 7601 Honeywell Ln, Bethesda, MD 20814

Appendix 2: The City of Seattle's experience with Inclusionary Zoning (IZ)

In April 2019, Seattle's Mandatory Housing Affordability (MHA) program took effect with the goal of creating thousands of new subsidized housing units made affordable through fees on development, while also boosting housing production overall. **It is on track to destroy Seattle's townhome construction activity.**

In exchange for a modest density bonus, builders have a choice between designating a certain number of units as income-restricted (defined as 65% of area median income or less) or paying a hefty fee. "Based on a 2021 survey of [builder trade group members in the area], the average MHA fee per townhome unit is $32,743, or $130,972 for an average four-unit project. This fee roughly doubles townhome predevelopment costs."

Consequently, new permits for townhomes have dropped precipitously, while they have remained about unchanged for the control group (see chart). We estimate that the effect of the IZ mandate was as high as an 80% reduction in townhome construction. Before the MHA implementation, townhome permits were averaging around 150 units per month and the trend was rising. By mid-2022, permitting had dropped to around 30 units with no commensurate drop in the control group.[2] (We notice a drop in both treatment and control group starting mid-2022, which may be because of rising interest rates.)

Many of the far-ranging consequences are summarized in an excellent report "The Decline of Seattle Townhomes Under MHA."

The lesson is that to be successful, reform needs to follow the KISS (Keep It Short and Stupid) principle.

For more details on the case study, see https://www.aei.org/research-products/report/expanding-housing-supply-with-light-touch-density-city-of-seattle-case-study/.

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[2] The drop was marginally smaller for projects with 2 to 4 units and larger for projects with 5 to 8 units.

Chart: Application Permits in the City of Seattle
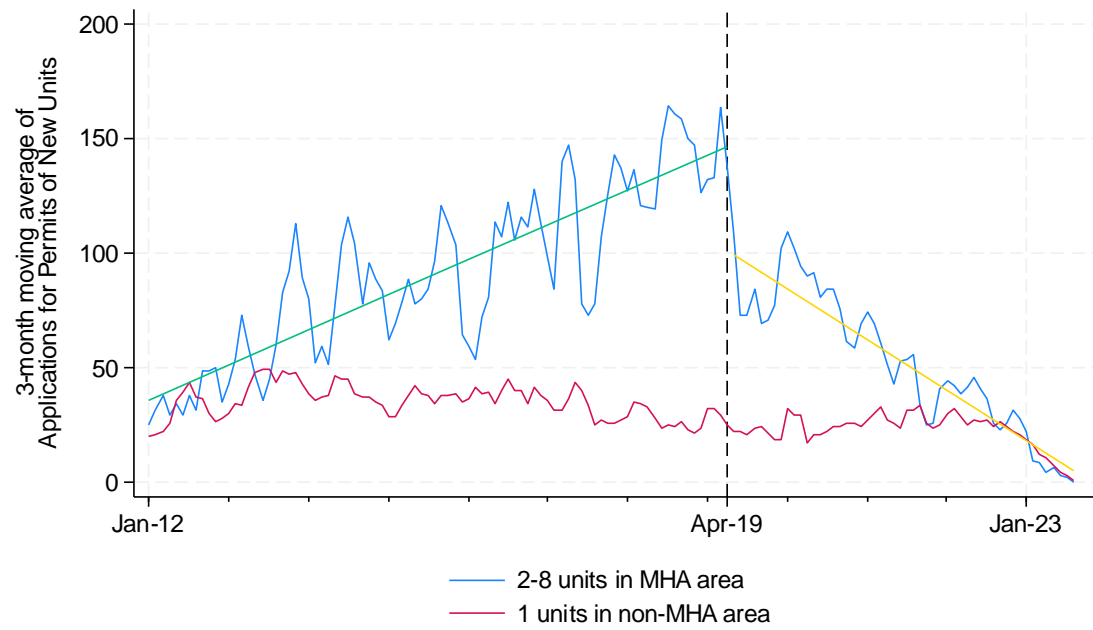
Source: City of Seattle, HUD, and AEI Housing Center, www.AEI.org/housing.

Appendix 3: Outcomes

Homeownership rates by type of building and year-built range.

Note: Middle Housing would be classified as SFA (single-family attached). Homeownership rates for Middle Housing are far greater than for multi-family buildings, particularly newly built ones.
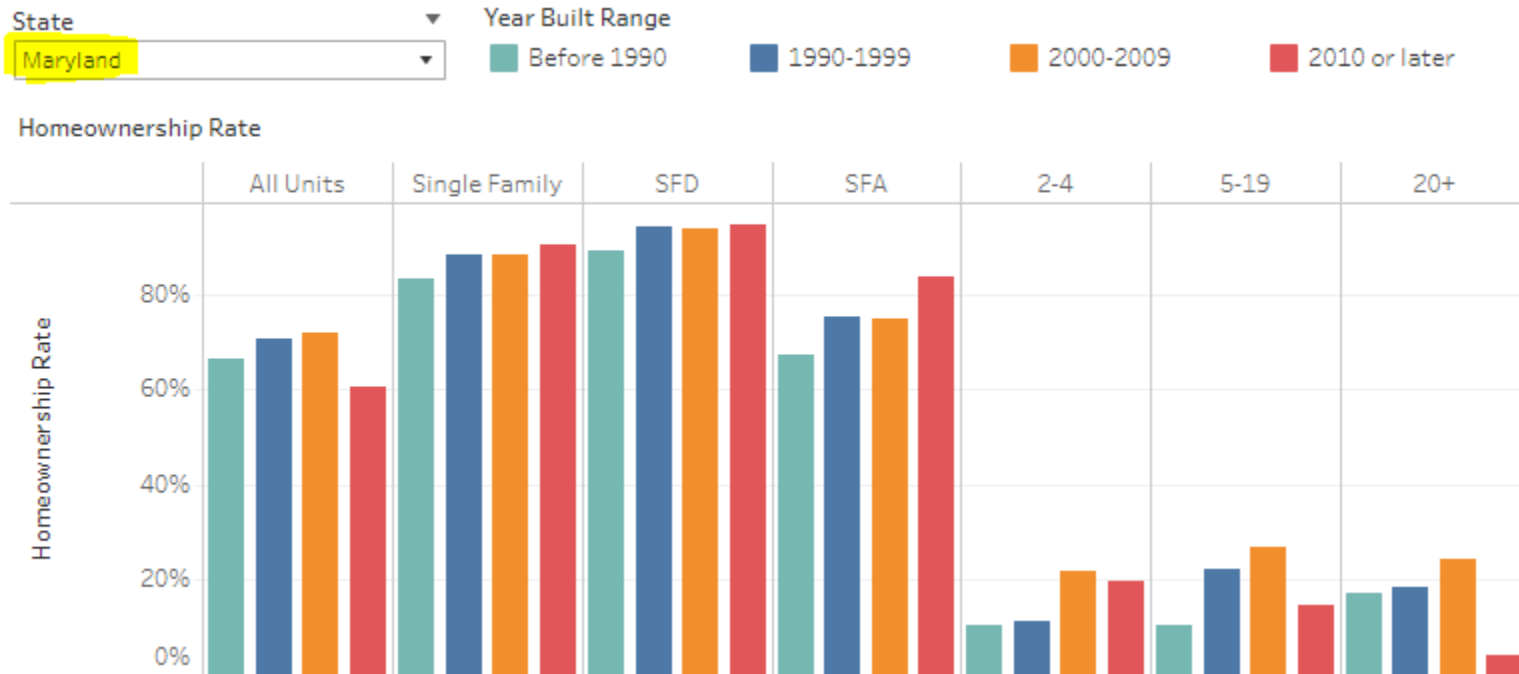

Rents and Property Values by type of building and year-built range.

Note: Middle Housing would be classified as SFA (single-family attached). Rents (after controlling for the number of bedrooms and location) after about near identical between Middle Housing and 20+ unit apartment buildings. Property values are lower, which enables homeownership opportunities as described above.

Controlled Contract Rent by Geography and Bedroom Count

	All Units	Single Family	SFD	SFA	2-4	5-19	20+
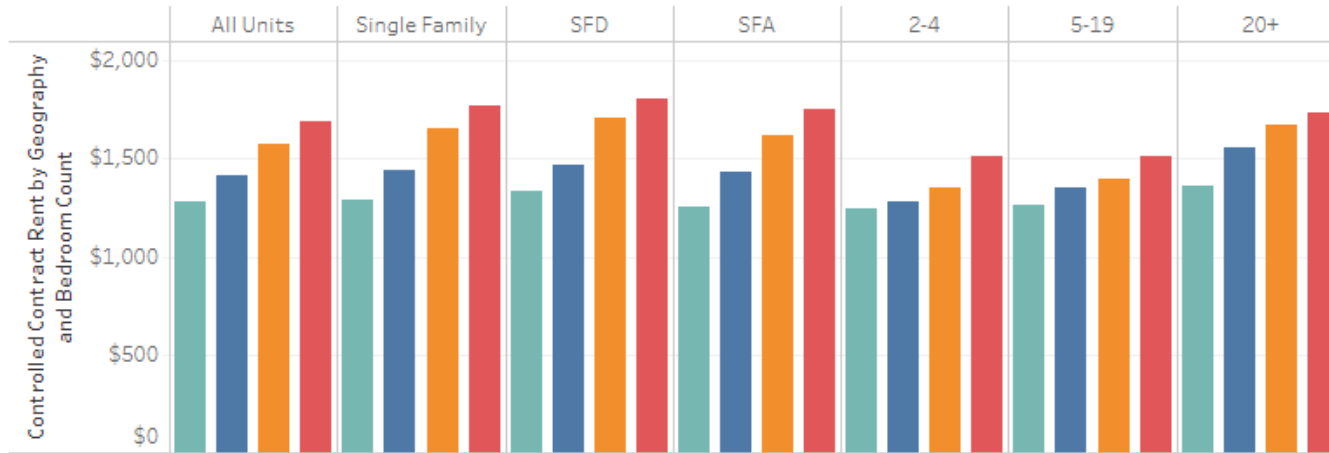
Controlled Property Value by Geography and Bedroom Count

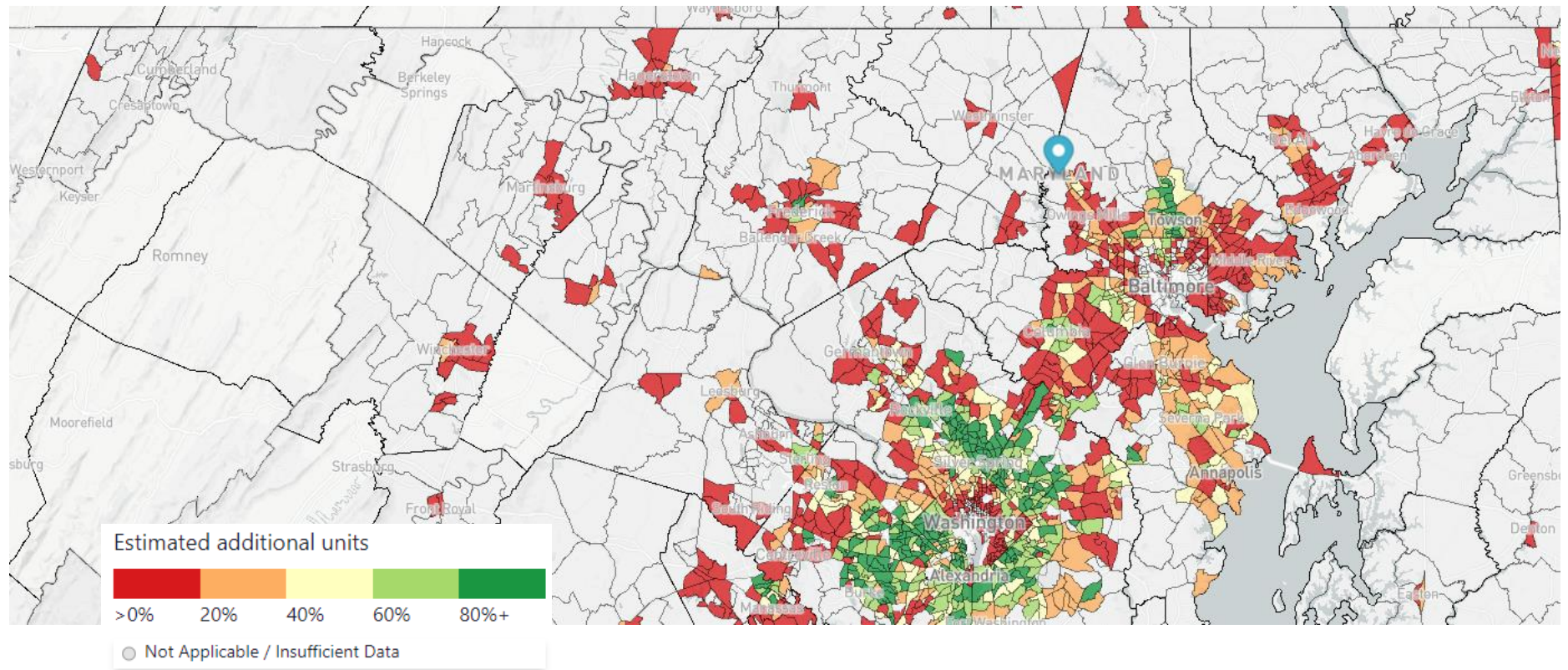|	All Units	Single Family	SFD	SFA	2-4	5-19	20+
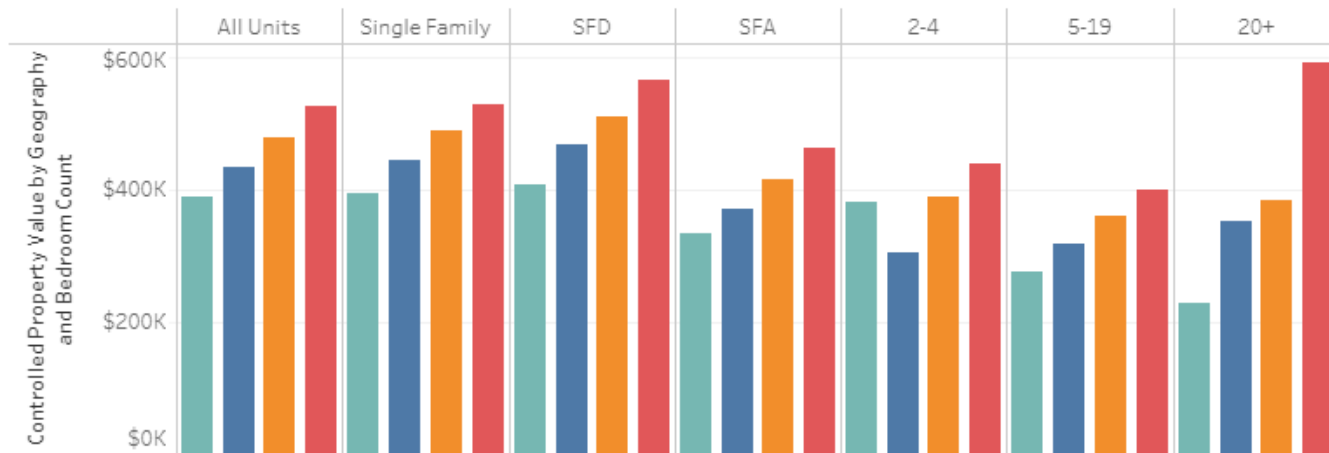
Note: For housing cost calculations, we exclude the bottom 5% of contract rents and property values and those households paying $0 in contract rent. We include all households to calculate the homeownership rate. We calculate all results using Census-created household weights. Rental or Property Values are suppressed if they have less than 10 unweighted observations for each state, structure type, year built, and tenure type category. The Controlled Property Values and Controlled Contract Rents by state, year built, and units in structure are generated using a state-by-state linear regression with controls for bedroom count and Public Use Microdata Areas.

Source: 2021 ACS 5-Year Microdata and AEI Housing Center.

Appendix 4: Census Tract Map of Middle Housing Potential

The map displays the Middle Housing potential in increasing the housing stock. The map assumes a maximum allowable density of 8 units per parcel.

For more, see https://heat.aeihousingcenter.org/ltd-map.

Estimated additional units

>0%   20%   40%   60%   80%+

⊙ Not Applicable / Insufficient Data

Note: Estimates are based on a maximum of 8 units on existing SFD parcels. For full county and state estimates, see our Light Touch Density Supply Estimates Tool.