OPENING SAN DIEGO’S DOOR TO LOWER HOUSING COSTS

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Since 2010, Point Loma Nazarene University’s (PLNU) Fermanian Business & Economic Institute (FBEI) has been actively engaged in providing consulting services to numerous individuals, for profit and non-profit businesses, government agencies, and organizations throughout the region, as well as nationally and internationally. In addition to being the Economic Forecasting Unit for California State Controller John Chiang for the past two years, other long standing partners and clients include, but are not limited to, San Diego Military Advisory Council (SDMAC), San Diego Zoo Global, Sempra Energy, Chain Link Fence Manufacturer’s Institute (CLFMI), The Corky McMillin Companies, National Association for Business Economics (NABE), Equinox, and San Diego Workforce Partnership.

In the following report, Opening San Diego’s Door to Lower Housing Costs, we attempt to quantify and present an objective analysis of the cumulative economic impact of government fees, regulations, and requirements on the cost of new single and multi-family housing, including both purchased and rented units, in various jurisdictions in San Diego County. For the purposes of this report seven jurisdictions were analyzed: Carlsbad, Chula Vista, the City of San Diego, San Marcos, Santee, other incorporated cities as a group, and unincorporated areas in San Diego County. The overall market is divided in four price tiers. In addition to the regulatory impact, we also look at the ripple effects of the regulatory environment, including the effect on households priced out of the market, the overall implications for population, business formation, jobs, and economic growth. We analyze the economic benefits that could accrue from a relatively moderate reduction in the regulatory costs restricting housing access. Additionally, we develop a set of best practices and present a set of actionable recommendations to improve the regulatory process regarding plan use, entitlements, and permitting, while at the same time preserving public goals and objectives but at a lesser cost.

We would like to thank the developers, builders, investors, community groups, council members, staff, and others who assisted us with obtaining accurate and timely information to include in our research, analysis, and recommendations for this report.

We appreciate the opportunity to present this study to individuals, firms, government officials, and decision makers at all levels. Our desire is that the results of our work will have a positive impact on a local level and will be used by elected officials to effect change in our region.

Cathy L. Gallagher
Executive Director
Executive Editor, Opening San Diego’s Door to Lower Housing Costs
Fermanian Business & Economic Institute
Point Loma Nazarene University
ABOUT THE AUTHORS

Executive Editor:

Cathy L. Gallagher – Executive Director, Fermanian Business & Economic Institute
Ms. Gallagher has extensive business experience as owner, manager, operator of several small businesses on the east coast before joining PLNU 11 years ago. In her current role Ms. Gallagher is responsible for overall leadership of the Institute, planning and implementation of all strategic initiatives, and building awareness of the many programs, services, and resources that further its mission and goals. She works closely with for-profit and non-profit businesses, organizations, and individuals, nationally and internationally, to develop collaborative, strategic, and mutually beneficial partnerships furthering objectives and bringing actionable results.

Ms. Gallagher provided editorial leadership of the Opening San Diego’s Door to Lower Housing Costs study, as well as oversight of the overall timeline and deliverables. She wrote the Letter to the Reader and Best Practices, and co-authored the Introduction.

Primary Author

Dr. Lynn Reaser, Ph.D. – Chief Economist, Fermanian Business & Economic Institute
Dr. Reaser has an extensive background in finance and banking as the former Chief Economist for the Investment Strategies Group of Bank of America and as a Chief Economist for Barnett Bank and First Interstate Bank prior to that. In her role at the Institute, she provides actionable economic counsel to PLNU and its stakeholders, as well as to the overall business community. She leads the economic research team of the Institute and is highly proficient at analyzing economic data, modeling, and forecasting, with special attention given to providing clear and concise recommendations for the reader. Reaser is a leading spokesperson for the university, conducting interviews with newspapers, magazines, television, radio, wire services, and the internet on a variety of topics related to the economy. She speaks at national and international conferences and forecasting events throughout the year. Reaser currently serves as the Chief Economist for California State Controller John Chiang’s Council of Economic Advisors.

Dr. Reaser provided oversight of the Opening San Diego’s Door to Lower Housing Costs study and was the lead author of the Executive Summary, Housing Regulation in the San Diego Region, The Economic Benefits of Regulatory Reform on Housing Access sections of the report, Recommendations, and Methodology sections with input from members of the team responsible for sub sections. Additionally, she co-authored the Introduction.
Contributors

**Peggy Crane, M.S.** – Economist, Fermanian Business & Economic Institute
Professor Crane is a skilled business economist and highly regarded economics professor in San Diego for more than twenty years. She has been an author and accuracy checker for Cengage Learning and Prentice-Hall Publishers. Prior to her work in academia, Crane worked as a Financial Analyst and Economist for San Diego Gas and Electric Company and for Home Federal Savings and Loan, with an emphasis on performing detailed financial analyses on new and existing products, services, and functions in the organization, and preparing written and oral reports for senior management. Crane joined the economics team at the Institute two years ago after many years of teaching at PLNU.

**Professor Crane conducted interviews with planning officials, builders, and developers to validate information for the Opening San Diego’s Door to Lower Housing Costs study. She was also responsible for calculating, summarizing, and writing the summary of the vertical and time costs associated with building a house and a co-contributor on modeling, calculating, summarizing, and writing of the Housing Regulatory Costs Across Various Jurisdictions section.**

**Dieter Mauerman, MBA** – Business & Economic Research Associate, Fermanian Business & Economic Institute
Mr. Mauerman has worked as a business & economic researcher at the Institute for five years. His responsibilities include conducting field research, data acquisition and analysis, and creating communication and presentations of the results of research and analysis for client projects and studies. Mauerman manages and directs individuals and groups of MBA student researchers who assist with studies and projects for the Institute.

**Mr. Mauerman conducted interviews with planning officials, builders, and developers to validate information for the Opening San Diego’s Door to Lower Housing Costs study. He also provided oversight of data collection and research for the Opening San Diego’s Door to Lower Housing Costs study, was responsible for all exhibits included in the report, and was the primary author of the Developments 101: Building A House in San Diego section of the report.**
**Mark Undesser, MBA** – Researcher, Fermanian Business & Economic Institute

Mr. Undesser has significant experience as a researcher, business strategist, analyst, and corporate sales trainer. He specializes in developing creative solutions for addressing business challenges in both for profit and non-profit sectors. Undesser joined the research team of the Institute two years ago as an MBA student and continues to work as a research analyst for projects and studies.

**Mr. Undesser was responsible for the compilation of data, quantitative analysis, and the build-out of the master spreadsheet to calculate cost percentages for the Opening San Diego’s Door to Lower Housing Costs Study. He was also the primary author of the Fees, Entitlement Costs, and Mapping Costs sections of the report.**

**Nic Herbig, MBA** – Researcher, Fermanian Business & Economic Institute

Mr. Herbig has worked in mortgage banking for the last few years, with Home Owners Association (HOA) issues in particular. He joined the economics team as an MBA student to assist with studies and projects.

**Mr. Herbig conducted interviews with planning officials, builders, and developers to validate information and gather data for the Opening San Diego’s Door to Lower Housing Costs. Additionally, he conducted research and analysis for various aspects of the project and was the primary author of the sections on Affordable Housing, and HOAs.**

**All authors participated in the planning process of the study and contributed to one or more sections, including the Recommendations and Methodology sections. Additionally, all participated in reviewing the data and findings, as well as the review of the final study.**
Acknowledgements:

Laura Yoccabel-Dibble – Assistant Director, Fermanian Business & Economic Institute
Ms. Yoccabel-Dibble brings a strong background in management, events, operations, and marketing to her position at the Institute. She is responsible for planning, management, and execution of all events for the Institute. Additionally she manages the independent contractors and student assistants who assist with studies and projects for the Institute.

Ms. Yoccabel-Dibble provided scheduling, instruction, and management to student assistants involved in the project.

Jacy Romero – Researcher, Fermanian Business & Economic Institute
Ms. Romero assisted with data collection and research for the project.

Laura Meng – Student Researcher, Fermanian Business & Economic Institute
Ms. Meng assisted with data collection and research for the project.

Scott Andrews – Provided layout and design for the project.
The Fermanian Business & Economic Institute

The Fermanian Business & Economic Institute (FBEI) is a strategic unit of the Fermanian School of Business (FSB) at Point Loma Nazarene University (PLNU) that specializes in expert business and economic consulting, modeling, forecasting, studies, research, commentary, speeches, business plans, and related services to firms, organizations, and individuals nationally and internationally. The FBEI also provides the San Diego region with economic forecasting events, business and economic roundtables, and special projects.

Through our partnerships and in our work with clients, the FBEI represents the academic standards of the university by maintaining a clear unbiased approach and has a reputation for authoritative insight and expertise regarding issues of business, economics, and policy facing our region. In addition to being the Economic Forecasting Unit for California State Controller John Chiang, other clients include, San Diego Military Advisory Council (SDMAC), Chain Link Fence Manufacturer’s Institute (CLFMI), National Association for Business Economics (NABE), Sempra Energy, San Diego Zoo Global, and The Corky McMillin Companies.
EXECUTIVE SUMMARY

• The total cost of regulation amounts to about forty percent of the cost of housing across the various price segments in all of San Diego County.

• Regulatory costs vary considerably by jurisdiction across the region. Based on the weighted average of sales and rentals, the costs range from about $125,000 (22%) in Santee to about $282,00 (44%) in Carlsbad.

• Regulatory costs include the statutory fees of building permits, sewer connections, water, schools, drainage, traffic, and other elements. Those are only a part of the total. Other regulatory costs occur throughout the entitlement, mapping, development, permitting, and homebuilding phases of a project.

• The time involved in what is often a prolonged and complicated process represents a major cost driver and can add 15% or more to the price of a new house. Projects where a master plan is not already in place can require 12 or more years before the first house is ready for sale.

• This study indicates that approximately 21% of, or about 233,000, households throughout San Diego County are priced out of the market for owned or rented housing based on their current incomes. These individuals may have other assets they can use or may be able to secure financial assistance from family or friends. They may find options in the stock of existing housing, although new home prices will probably have an impact on that part of the market as well. If those options are not available, they may be forced to share housing with others in the region or find housing outside the area.
• A relatively modest 3% reduction in the regulatory cost of San Diego’s housing could open up housing alternatives to approximately 6,750 additional households in one year.

• The economic benefits of the resulting increase in homebuilding would be substantial. After including all of the ripple or multiplier effects, San Diego could realize a $3.1 billion gain in its gross regional product (GRP) and a $2.5 billion gain in its total personal income. An additional 37,000 jobs could be created.

• San Diego County’s recent trend of net domestic out-migration of about 11,000 residents per year could be reversed to a net positive inflow of about 7,000. This would add to other sources of population growth (births minus deaths and foreign immigration).

• Regulatory reforms that could preserve public objectives, but at much lower cost, include: establishing benchmarks for project and permit approval times, replacing full cost recovery by a flat fee for mapping costs, standardizing building codes for all jurisdictions in the County, disallowing additional challenges and reviews once a project is approved, and establishing a sliding scale for affordable homebuilding requirements to recognize the importance of economies of scale.

San Diego’s prime coastal location will always mean a relatively high base of land values, but many dimensions of the regulatory process inflate housing prices while accomplishing little or no benefit. Reasonable solutions can and should be implemented to pare down the cost of housing, which has been the greatest single challenge to the fulfillment of San Diego’s potential.
Regulatory Costs Drive 40% of Average New Housing Costs in San Diego

Thousands of dollars

Exhibit 11

Source: FBEI

Average Price Average Regulatory Cost*

0 100 200 300 400 500 600

*Weighted by total units rented or sold in 2013

21% of San Diego Households Priced Out of the Market

Percent

Exhibit 29

Source: FBEI

21% of San Diego Households Priced Out of the Market

Regional Distribution of Economic Benefits from 3% Easing of Regulatory Impact

Increase Percent

Gross Regional Product, $ bil $3.15 1.7%

Personal Income, $ bil $2.54 1.5%

Employment 37,331 1.9%

Business Enterprises 1,372 1.7%

Population 18,222 0.6%

Housing Permits 6,749 75%

Economic Impact of 3% Average Reduction in Regulatory Costs

Source: FBEI
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I. INTRODUCTION

Housing represents one of the most important issues facing all San Diegans. For every $100 of spending, a typical household in the region spends nearly $40 on shelter. In contrast, food accounts for only about $12 of that $100 budget.

General agreement exists that housing should be safe, while a high quality of life is attained and the environment is protected. At the same time, housing should be affordable. These objectives often clash in practice. A plethora of regulations and their implementation, while well intentioned, may have aggravated San Diegan’s access to housing.

This study is not presented as a sounding board for industry complaints against public regulations and officials. Rather, it seeks to understand the true expense of the regulatory process and to find ways to reduce those costs while achieving goals in the public’s interest.

Seven jurisdictions were analyzed: Carlsbad, Chula Vista, the City of San Diego, San Marcos, Santee, other incorporated cities as a group, and unincorporated areas in San Diego County. The overall market is divided in four price tiers:

- $0-300k
- $300-450k
- $450-600k
- $600k +

For rental units, the price equivalents were calculated based on the comparable monthly and annual payments that would be required under conventional mortgage and lending standards. Both single-family and multi-family housing markets were investigated.
In 2013, sales and rentals totaled 4,040 new housing units throughout San Diego County. (See Exhibit 1.) Of this total, 55% were multi-family or attached housing. (See Exhibit 2.) Rentals accounted for 43% of the total new units that were absorbed into the marketplace or occupied.

Our study begins with an overview of the process of building a house in San Diego, including several aspects of the regulatory process. We explore the details and effects of each major type of regulation, the costs involved, and the impact on households in the seven jurisdictions studied in our report.

We then project the annual economic impact on the region if the regulatory process were reformed to reduce average regulatory costs by just 3%. The effects on gross regional product (GRP), personal income, employment, the number of business enterprises, population, and housing permits are presented for the aggregated region of San Diego County and its major jurisdictions.

Recommendations to help narrow the affordability gap due to the regulatory process, as well as a set of best practices, conclude our study and are presented as a set of actionable and practical steps to effect change in our region.

An overview of our methodology used to prepare the study and a full list of references are provided at the end of the report.
II. DEVELOPMENT 101: BUILDING A HOUSE IN SAN DIEGO

Constructing a residence in San Diego, whether a single-family house that might be bought or an apartment that might be rented, involves a complex process with many different elements. Significant amounts of time, planning, and resources are required between the point where a housing project is conceived and when a dwelling unit is delivered to the marketplace.

This process, including the interaction with various regulatory agencies, their staffs, policymakers, and the public, can be split into five distinct phases: entitlement, mapping, infrastructure, permit review, and construction. (See Exhibit 3.) Some of these elements frequently overlap. Since the entire process is very time consuming and can take several years to complete, projects will often switch ownership a few times before any structure is actually built. Different developers or builders acquire expertise based on a specific skill set or process in the entitlement, permitting, or building phases.

![Exhibit 3: Phases of Home Building*](image-url)
Entitlement

The “raw” land available for development can come from three sources: vacant land, land that is being redeveloped from housing that was previously onsite, or land that is being converted from other uses, such as commercial, retail, or industrial. The entitlement phase involves:

- Taking a piece of land and securing approval for a master plan if not yet in place
- Making any necessary amendments to the master plan
- Securing an Environmental Impact Report (EIR) if required
- Developing mitigation plans for effects on elements ranging from water to traffic
- Drafting a tentative map for the particular project

For the purposes of this study we have used the term “master plan” to designate an area of land within a jurisdiction that has an entitlement approval already in place that allows for suitable development within the given area. A master plan entitlement is a greater and more specific level of entitlement than a City’s general plan. Specific plans, community plans, and sectional planning area plans (SPAs) all fall within the master plan definition of this study.

Many times a jurisdiction will have a master plan already in place. A master plan lays the basic ground work for how a community will be developed in the future. This includes assigning zoning requirements for certain areas, determining how certain areas will be used, and other dimensions. The whole process can take several years to complete and may face significant resistance from the public, special interest groups, and other national, state, and local agencies. Because of this high risk of opposition, financing options for a project in this stage are mostly limited to private investors requiring high returns.

Many times, particularly if a master plan has not yet been adopted, an EIR must be completed. The city often hires a consultant to complete the EIR and prevents any communication with the developer despite the fact that the developer is required to pay for the work and may possess valuable information. If this is the case, it is advantageous for the developer to hire his own consultant to complete an EIR because it provides the developer with the tools to defend his planned project.
If a master plan is already in place, the entitlement phase typically takes about 3 years. If a plan is not in place, the process will generally involve 8 to 10 years. Once a master plan, site plan, an EIR if necessary, and a tentative map have been completed and approved, the project moves on to the mapping phase.

The California Environmental Quality Act (CEQA) applies to most public agency decisions to carry out or approve both private and public projects. The objective of the CEQA process, enacted in 1970, is to disclose to decision makers and the public significant environmental effects of the proposed project and to identify ways to avoid or minimize those effects. For projects that may result in significant environmental impacts, CEQA requires preparation of an environmental impact report.

CEQA is not a substantive regulatory statute. Instead of prohibiting jurisdictions from approving projects with significant impacts, CEQA requires that the decision makers and public be fully informed about the impacts, allow public comment, and avoid or reduce the impacts when feasible.

A jurisdiction has certain, limited latitude in deciding whether impacts of a project are significant by adopting “Standards of Significance” thresholds. However, any significant thresholds must establish whether a project would cause a substantial or potentially substantial adverse change in the environment. In addition, jurisdictions have latitude in deciding who will prepare the CEQA analysis, including the jurisdiction staff, a jurisdiction consultant, or an applicant’s consultant. Regardless of who prepares the CEQA analysis, the jurisdiction ultimately is responsible for its contents and compliance with CEQA.

California is one of only 15 states that have a mandated environmental review process such as CEQA.

Most litigation involving a project entitlement process is based on CEQA. Project opponents typically claim the CEQA documents have failed to identify and analyze all environmental impacts. CEQA litigation abuse is well documented. The burden to bring a suit is small. When plaintiffs prevail in their CEQA litigation, they typically recover legal costs and fees. However, when project proponents and jurisdictions prevail, the ability to recover damages or fees from suits is severely limited.
Mapping

The mapping process generally takes less time and is less risky to potential investors and developers than the entitlement phase. Because of this, more financing options for a project are available at a lower cost to the developer or builder. The cost is still considerable. The services required to perform the mapping and engineering services can include civil engineers, soil consultants, planners, landscape architects, attorneys, and environmental consultants. Most of the work is done by consultants on a relatively tight timeframe.

The regulatory costs involve the review and processing of various documents by individual cities, including changes in plans for grading, drainage, landscaping, parks, and other issues. A number of rounds of changes, new approvals, and further changes are often experienced. The mapping stage typically requires about 12-18 months to complete.

Infrastructure

The development process involves providing grading, drainage, and other functions to prepare the site for building. It then entails installing all of the infrastructure necessary to convert raw land to finished lots. This phase includes building the water, power, sewer, and communications lines, as well as the streets, lighting, and other elements that are a critical part of a project. These various improvements to the raw land are the “horizontal” dimensions of the project. Additional requirements may be imposed beyond the improvements a builder would implement to meet the expected demands of a given community. These might include, for example, the construction of additional private or public parks and facilities.

Fee credits are sometimes given to partially offset the cost of public facilities like parks or trails. Such fee credits may trigger prevailing wage mandates (not included in this study because of ongoing litigation and changes in state law).

If a public park is not built for a development project, then park-in-lieu fees are required. These public open spaces may also require an endowment and perpetual management to maintain the area. Some jurisdictions may require off-site open space to be set aside as a condition of the project being approved. Many jurisdictions also are beginning to require private Home Owners Associations (HOA) parks and facilities for recreational purposes in addition to the public areas.

The entire development process, involving various improvements to the raw land, typically requires about 8-18 months, with the typical length equal to about a year.

Upfront infrastructure financing is a major problem, particularly in a tight credit market. Developers can face severe restrictions on bond financing and high infrastructure burdens before home sales occur.
The review of the housing permits required to begin construction averages about 6 months in most parts of San Diego County. Once the required permits are secured and all necessary fees paid, construction can begin. Regulatory impacts at the building phase can involve, for example, the requirement that certain building standards above those mandated by state law be met. These are the additional “vertical” costs of a project. A house can usually be built in about a year. (A single-family home can often be built in 3-6 months, while a multi-family unit will generally require a year to 18 months.)
Developers and builders face a labyrinth of regulatory hurdles as a project is moved from the conceptual phase to a dwelling that is ready for occupancy. The statutory fees required for a building permit are only one dimension. The difference between the expenses and procedures that might be posted on the official documents or websites of various jurisdictions and their actual implementation can often be significant. How various laws or regulations are interpreted or implemented can vary widely according to the particular public official involved with a specific project.

Seven different aspects of regulatory costs are analyzed in this section: entitlement costs, mapping costs, eliminated units, fees, affordable housing requirements, vertical construction costs, and time costs. In addition, the trend towards mandates for HOAs is discussed.

**Entitlement Costs**

Entitlement costs and time vary greatly depending on a variety of different factors, such as whether or not a master plan has been completed by the time the builder purchases the land. The entitlement phase differs from jurisdiction to jurisdiction and can range anywhere between two and ten years (an average of eight). The entitlement phase of a development with a completed master plan can be considerably less in some jurisdictions. The variation from jurisdiction to jurisdiction makes it difficult for the developer/builder to budget and plan for a project. Because capital is tied up for extended periods of time, a developer/builder must be financially strong to endure the regulatory process before he starts to see a return on investment many years later.

The entitlement process is not only the most time consuming compared with other elements but also carries the largest cost of capital. The average cost of capital is 18-20% for projects without a master plan. Projects with a master plan carry (on average) an 11% cost of capital. Either way, prolonged delays translate into millions of dollars in extra cost that ultimately increases the price of the house.

High rates of interest within the industry are necessary due to the inherent risks and delayed return associated with raw land development and the lack of access to financial markets. Private lenders require anywhere between a 20-22% Internal Rate of Return for initial entitlements and a 7-8% rate is typical from banks once a tentative map is in place.

Time delays are common due to bureaucracies that lengthen the time to final approval.
A conflict of interest exists within the system due to the fact that there is no incentive for municipalities to work more efficiently. City and county officials are paid by the hour instead of by some metric that rewards effective and efficient performance.

Redundancy within the system is another constraint that adds to housing costs. Even after a master plan is approved, that approval can easily be overturned at a later date if an official sees even a minor deviation from the plan. This frequently happens when employee turnover within the county/city results in the assignment of a new reviewer to a building project. The overturning of the initial approval leads to more delays.

Local policy “add-ons” to CEQA exist in the San Diego Municipal Code. These “add-ons” allow for additional appeals and public hearings on CEQA far beyond what CEQA requires. Every time an appeal or public hearing occurs, added regulatory costs are assumed by the developer, which is ultimately passed on to the consumer.

Within the City of San Diego for example, there are five different processing “levels” for project approval: 1) Staff Approval (ministerial), 2) Staff Approval with Appeal, 3) Hearing Officer (discretionary), 4) Planning Commission Approval (discretionary), and 5) City Council Approval (discretionary). Discretionary levels of approval require CEQA review which allows for challenges to the environmental determination. Except for Process 1 (Staff Approval), the remaining levels of approval involve a public process that may result in reversing a previous approval requiring the project to start over. A project may be approved by the Hearing Officer only to be appealed to the Planning Commission where the appeal is upheld, resulting in a project denial. The appeal process may add several months to over a year of additional time and cost which adds to the final expense of housing development.

Regardless of these challenges, some jurisdictions are easier to work with than others. The data on time cost suggest some jurisdictions have relatively quicker turn-around in the approval process. Of the seven jurisdictions we studied, Chula Vista, San Marcos, and Santee have the lowest time costs.

The most expensive component of the entitlement process arises from conducting the Environmental Impact Report (EIR). Time cost makes up the majority of this expense. Developers are highly motivated to ensure the EIR is done correctly because any time setbacks from a badly done EIR can be extreme. If a developer skips this process and is sued, all work must cease until the matter is resolved, however long it takes. Even if the city does its own EIR on a project, the developer is still motivated to do his own since the municipalities are not held liable for any damages. The sole burden of liability rests on the developer/builder.
On average, entitlement costs due to regulation are approximately $4,500 per unit and represent about 1% of the price of the home. This figure excludes time costs associated with regulatory delays in the entitlement process. Costs from delays are accounted for under the “Time Costs” section of this report. There are also some relatively minor statutory costs for entitlement paid at the time the building permit is issued. These costs are included under the “Fees” section of this report.

**Mapping Costs**

Mapping costs contain inefficiencies similar to entitlement costs. Delays occur every time an official adds new comments to the mapping plan. It is not atypical for new comments to be added even after the plan has been reviewed and approved several times. Due to this inefficiency, some jurisdictions (unincorporated) have created a “No Late Hits” policy. This process helps suppress relatively minor issues from causing major delays in the approval process. If an issue of major importance comes up, the comment is expedited to upper management or to a hearing. While this policy does help reduce inefficiencies, it does not guarantee that the developer will not experience other types of delays. As mentioned earlier, municipal employees have no incentive to complete their reviews in a timely manner because they are paid hourly and not incentivized to work more efficiently.

Another problem that adds to mapping costs is that infrastructure standards vary vastly. Different jurisdictions have different road building standards which lead to inefficiencies. The lack of a universal standard across the County makes executing the mapping phase much more difficult than it needs to be. Some cities allow developers to hire their own engineering consultants to help expedite the process. Other jurisdictions require city-hired consultants to sign off on plans. This adds additional costs to the developers because they wind up hiring their own engineers to ensure the work done by the city-hired consultants is accurate. This is crucial since the developer is held liable for any mistakes or errors, not the municipality. Even when a developer does hire a consultant, reconciling information between parties is extremely difficult because no communication is allowed between the city-hired consultant and developer’s consultant. This causes misunderstandings, frustration, and more costs.

On average, mapping costs due to regulation are approximately $4,000 per unit and represent about 0.89% of the price of the home. This figure excludes the time costs associated with delays at the mapping stage. Costs from delays are accounted for under the “Time Costs” category of this report. There are also some relatively minor statutory costs for mapping paid at building permit. These costs are included in the “Fees” section of this study.
Eliminated Units

A certain percentage of units are typically eliminated from a project early in the entitlement phase to meet various demands for more open space. While some of these requirements represent the implementation of federal and state laws, local jurisdictions may impose additional set-aside requirements. The cost of these potential units is ultimately borne by home buyers and renters.

In San Diego County, the share of eliminated units is under 5% in San Marcos, but is around 15% in Carlsbad and Chula Vista. (See Exhibit 4.) In the unincorporated areas of San Diego County, 10-15% of potential units are typically eliminated. In the City of San Diego, as much as a third of potential units can be cut out of a project’s potential.

The higher land values in such areas as Carlsbad and the City of San Diego mean a higher opportunity cost for each housing unit foregone or given up. The impact on housing prices of eliminated units is around 4% in the housing price range of $450,000 to $600,000 in both Carlsbad and the City of San Diego. In contrast, the impact on housing prices of mandated unit elimination is generally less than 0.5% in San Marcos.

Exhibit 4

Land Use Policies Eliminate Potential Housing

Share of potential units, percent

Source: FBEI
Fees

Statutory fees levied by a jurisdiction are most often collected at the time the building permit is issued. Most jurisdictional fee programs encompass two different types of fees.

The first include fees that are levied to offset the project’s impact on regional infrastructure. For the purpose of this study, we refer to these fees as “horizontal costs.” Horizontal related fees represent the largest component of total fees. Fees levied in this category include:

- Park fees
- School fees
- Water fees
- Sewer fees
- Drainage fees
- Transportation related fees
- Police, fire, library, and other public administration fees

Most of the fees associated with this category are created by the jurisdiction after adopting a study that analyzes current and projected infrastructure needs of the region, taking into account future growth projections and current infrastructure capacity. Under State law a jurisdiction is not allowed to levy a fee on future development to make up a city’s infrastructure deficit unless the project has a specific impact that caused the deficit. Because of this requirement, it is incumbent on the jurisdiction adopting an infrastructure study that results in developing a fee for new projects to clearly distinguish “unmet need” from “future need.”

The second type of fees levied under horizontal costs relates directly to the type and size of buildings that are to be constructed. These fees include:

- Plan check fees
- Building permit fees
- Trash recycling fees
- Inspections fees
- Seismic fees
On average, total fees amount to approximately $54,000 per unit and represent about 11.75% of the price of the home. Significant variation exists across jurisdictions and price segments. (See Exhibit 5.)

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<th>$450-$600</th>
<th>$600-&gt;</th>
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<td>$61,402</td>
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</table>

Source: FBEI

Affordable Housing

Affordable housing mandates have been put in place to provide for those individuals and families deemed unable to afford market-rate housing within a specified location. The cost associated with the affordable housing requirements, in reference to project developers, can include the donation of developed land or payment of an in-lieu fee.

While in-lieu fees are generally available, they often are not cost effective and not used. They often are based on the cost of a median priced home currently for sale in the surrounding areas rather than the cost of an affordable housing unit.

Where the developer is forced to build, rather than pay in-lieu fees, a number of inefficiencies make the provision of affordable housing very expensive. Some jurisdictions require “like kind” affordable housing, such as for-sale affordable units or excessively large rental units. Examples include Vista and Encinitas.

The cost of affordable units may be very high as they are subject to special design requirements such as higher Title 24 requirements which are California’s Building Standards Code, include energy efficiency requirements. If the project is less than around 50 units, it also will often not operate efficiently and will have high operating expenses. The homebuilder will be required to both donate the site and often to pay in cash the remaining cost of the project if debt and tax credit equity are insufficient to fund the project.
The basic percentage of affordable housing units mandated is generally 10% of the number of market rate units developed, as seen in the City of San Diego, Chula Vista, and other incorporated cities within the County. The cities of Carlsbad and San Marcos have the highest threshold of 15%. The City of Santee and unincorporated areas of San Diego County do not have an affordable housing mandate in place at this time. (See Exhibit 6.)

In addition to these base numbers, it is common for each municipality to negotiate for a larger percentage of affordable housing units. This can increase the percentage of affordable units up to 12% or 18% of the number of market rate units depending on the municipality in question. For the scope of the study only the basic, most conservative numbers were utilized.

Due to the 15% requirement in San Marcos and Carlsbad, market rate homes in these communities bear the largest effects of the affordable housing mandate. The cost of the fully developed land and cash contributed by the developer in Carlsbad is passed on to the final sales price of the remaining units, which accounts for 8-9% of the total sales price. Attached homes priced from $300,000 to over $600,000 face a price premium of 8%, while detached units in the $450,000 and higher range experience a 9% increase in price. The City of San Marcos has a range of 6-7% in price premiums because of the affordable housing mandate across its various cost brackets.
Vertical Construction Costs

Vertical costs included in this study are defined as costs associated with requirements adopted by federal, state, and local governments to build any type of structure. The types of regulatory cost that typically impact vertical construction are storm water runoff requirements, building code requirements brought about by a change of the code, and Title 24, or energy efficiency requirements.

Storm Water Requirements

In 2000 the San Diego Regional Water Quality Control Board revised and adopted a new storm water permit that significantly increased the cost of all new construction. Implementation costs were approximately doubled at that time. The permit was revised again in 2007 and included measures that again doubled the cost for implementation over the prior requirement. In 2014 the permit was again revised and the new requirements mandated in the new additions are required to be implemented by December 2015. While costs to meet the new requirements are not completely refined at this time, early estimates are that they could impact cost approximately 200% above current requirements. In addition, they will require further land set asides to address water quality filtration requirements.

Building Code Updates

Most jurisdictions follow the International Building code, formally the Uniform Building Code. However, many jurisdictions have latitude as to when they adopt the new or revised code. This is an important consideration in the regulatory cost of building any type of projects as projects that are already in some phase of construction when a code is revised can see significant increase in time and cost associated with meeting new requirements.

Title 24

Title 24 of the California Code of Regulations (also known as the California Building Standards Code) is a compilation of three types of building criteria from three different origins:

- Building standards that have been adopted by state agencies without change from building standards contained in national model codes;
- Building standards that have been adopted and adapted from the national model code standards to meet California conditions;
- Building standards, authorized by the California legislature, that constitute extensive additions not covered by the model codes that have been adopted to address particular California concerns.”
Part 11 of Title 24 specifically addresses the California Green Building Standards Code (CALGreen Code) and was the first statewide green building code in the United States. Many builders throughout San Diego County incorporate features into their new residential construction projects that are at least 15% above current Title 24 standards. In some cities, such as Chula Vista, builders are required to do so.

One of the regulatory challenges faced by builders in San Diego County is that Title 24 requirements are updated on a triennial basis. For example, the most recently revised regulations were put into effect on July 1, 2014. Builders with projects that have not been completed at the time of one of these updates may find that they need to have their project repeatedly reviewed to meet any revised Title 24 requirements. These repeated reviews can be costly and ultimately raise the price of new homes.

California has one of the strictest energy efficiency requirements in the United States, despite being the state with the mildest climate. Over the last nine years the State of California has increased its Title 24 Standards by 55%. The Governor has set a goal for all residential construction to be net zero on energy usage by 2020. This means that a building’s annual energy consumption must equal its annual production of renewable energy. As these requirements have increased, builders have been challenged with finding new and cost effective ways of implementing the standards. When the regulations first were adopted, builders often increased insulation and included energy efficient appliances and lighting fixtures. However, with each subsequent update, the cost associated with fulfilling the requirements becomes disproportionate to the gain and builders have not been able to pass on this cost to the consumer.
It was determined that vertical costs due to regulartory requirements, on average, add approximately $2.65 per square foot for new homes built in San Diego County. For example, vertical costs for a detached home sold in Chula Vista in the $600,000 and up price range are approximately $10,300 as a result of Title 24 and other mandated energy efficiency enhancements. On the lower end, the vertical costs associated with an attached home sold in the $300,000 and less price range in the City of San Diego and in San Marcos are approximately $2,400 since the average square footage of these homes is significantly smaller. For the average new home built in San Diego County, vertical costs represent around 1% of the price of the home. (See Exhibit 7.)

Exhibit 7

<table>
<thead>
<tr>
<th>Jurisdiction</th>
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<th>$450-$600</th>
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<td>$3,853</td>
<td>$7,150</td>
<td>$9,145</td>
</tr>
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</table>

Source: FBEI
Time Costs

Time cost is typically the largest cost associated with residential real estate development and it can have a profound impact on the types and locations of projects undertaken. Factors such as the existence of a master plan, environmental opposition, and local regulatory approval procedures can all greatly influence the overall cost of capital for a given project, which ultimately helps to determine whether or not homes will be built in a given area. (See Exhibit 8.)

One of the worst case scenarios in terms of time cost is for a residential development project to be proposed in an area where no master plan exists, particularly in a jurisdiction with an entitlement phase that is unusually lengthy as a result of convoluted regulatory approval practices. The high level of uncertainty and risk associated with the entitlement phase in areas where no master plan exists leads to the inability of developers to tap into financial markets until after a tentative map is completed, resulting in a cost of capital in this phase of approximately 18%. This high cost of capital coupled with an entitlement phase lasting nearly ten years in some jurisdictions results in a staggering overall cost of capital for such development projects.
Of the jurisdictions included in this study, Carlsbad and the City of San Diego are perceived to be particularly prone to high time costs under the circumstances outlined above. For example, attached homes built in Carlsbad in areas with no master plan were estimated to have average time costs ranging from $77,363 (17% of average home price) for homes in the $300,000 to $450,000 price range to $292,871 (34% of average home price) for homes in the $600,000 and up price range. Correspondingly, detached homes built in the City of San Diego in areas with no master plan in the $450,000 to $600,000 price range were estimated to have average time costs of $169,933 (30% of average home price). By comparison, attached and detached homes built in Chula Vista --- where all homes were built in master planned communities with a presumed cost of capital of 11% percent paid during a four year entitlement phase --- were estimated to have time costs of between 4% and 7% of the average home price.

(See Exhibit 9.)

Existing public policies encourage builders to build in less politically sensitive areas of the County and/or where a large master plan has already been approved. As one builder stated, “With greater time there is greater risk and higher cost. When considering the highest and greatest use, the shortest processing time is often considered heavily.”
In 1978 California voters passed Proposition 13, which put a cap on the amount of property tax that could be levied by on real property. The cap set in the statute is 1.1% of assessed value, with a limit preventing a rise to no more than 2% annually. Since the enactment of Proposition 13, counties and cities in California have struggled to find ways to maintain infrastructure that was formally paid for by simply raising property taxes.

Two methods that have been initiated since 1978 have been the use of Infrastructure and Maintenance Financing Districts and the creation of Homeowners Associations (HOAs).

Community Facility Districts (CFDs) and Mello Roos Districts are means by which physical improvements or maintenance obligations for an area or project are financed through an issuance of a public bond offering. The bond is secured by a lien on the property within the district and each property is then charged an additional property tax amount. It is not uncommon for property tax percentage rates with a public finance district to be double that of a property without a district.

CFDs and Mellos districts have been used to finance roads, public utilities (water, sewer, drainage, and power), parks, and schools.

Homeowners Associations or Common Interest Developments (CIDs) have their genesis back to 1964 and were initially utilized for governance and maintenance of common interest subdivisions or condominiums. Under a Home Owners Association, each property is governed by a set of Conditions, Covenants and Restrictions (CC&Rs) that set forth rules, regulations, and obligations within the CID. They also determine a monthly amount that each property owner must pay for so that the association can meet those obligations.

What the development of HOAs does to the home buyer is price more individuals out of the market. HOA dues must be included in the debt/income ratio when applying for a mortgage, along with taxes and insurance for the home. Increased documentation may also need to be collected by the lender such as the CC&Rs, insurance policies, and the annual budget.
IV. HOUSING REGULATORY COSTS ACROSS VARIOUS JURISDICTIONS

The regulatory climate faced by builders and developers varies significantly across the various cities of San Diego and its unincorporated areas under the jurisdiction of the County. This study quantifies the total costs of regulation in its various dimensions in each area.

Overall Comparison

The total cost of regulation amounts to about 40% of the cost of housing across the various price segments in all of San Diego County. (See Exhibit 10.) Regulatory costs vary considerably by jurisdiction and by price segment across the region. For example, in the $300-450 thousand price segment (the segment representing the largest number of new housing units sold or rented in 2013), costs average about $169,000, equal to 43% of the average $392,000 home price. (See Exhibit 11.) As a percentage of average home prices or rental equivalents, the shares range from about 22% in Santee to a high of 47% in the City of San Diego. (See Exhibit 12.)
The ultimate impact of housing regulations falls on the households who cannot find accommodations to purchase or rent given their incomes. Some households may be able to pay for housing out of their accumulated wealth in the form of stocks, real estate, or other assets. Others may be able to borrow from family members or friends to be able to afford San Diego housing. Finding alternatives in the existing stock of housing may be another option, but increases in the price of new housing will put upward pressure on the prices of older or existing units as vacancy rates decline. Affordability is likely to deteriorate as home prices rise faster than wages. Households without these opportunities will be forced to share housing with others or leave a particular area in search for less expensive housing elsewhere.
This study estimates that about 27% of households in Carlsbad are priced out of housing by various regulations. In the City of San Diego, regulations have blocked about 26% of households from housing affordable according the the distribution and levels of incomes in the area. In Santee and the unincorporated areas of San Diego County, the ratios are about 11%, which still represent large numbers of individuals. (See Exhibit 13.)

Exhibit 13

Households Priced out of San Diego Housing
Share of total, percent

Source: FBEI
Carlsbad

Carlsbad has one of the highest regulatory cost burdens included in the price of housing at about 42% to 46% depending on the price segment. This burden is borne by homeowners and renters in all price segments of housing. (See Exhibit 14)

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<th>Weighted Price</th>
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</thead>
<tbody>
<tr>
<td></td>
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<td>43.25%</td>
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<td>46.51%</td>
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Time costs represent the largest single driver of the regulatory total. For the $450-600 thousand price tier of housing, time costs account for approximately 47% of the total regulatory burden (See Figure 15.) and represent about 21% of the average home price in this bracket. The cost of financing the project through the entire process of various applications and approvals is substantial. The absence of a master plan in place for various projects and the city’s lengthy period for mapping approvals are principal factors driving this expense.

Carlsbad’s second largest element in its regulatory cost total involves the various fees that are imposed and collected when the building permit is issued. These fees add about 9% to the cost of housing. Another 8% of housing prices comes from the city’s requirements to provide affordable housing.
Across its various price tiers of housing, Chula Vista’s regulatory costs account for between 27% and 36% of average home prices. (See Exhibit 16.)

Fees are the largest component of regulatory costs, representing about half of those expenses. (See Exhibit 17.) For the $300-450 thousand price tier of housing, fees add about 17% to the average cost of housing.

Although time costs are not inconsequential and add about 5% to the typical price or rental equivalent of a new home, they are much less than in areas such as Carlsbad. The primary reason for this divergence is that master plans for developments are already in place.

Requirements to provide affordable housing are the third most important regulatory element. Although some households benefit from this provision, others face the likelihood of higher home costs.
Regulatory costs are relatively high in the City of San Diego, representing between 34% and 51% of the average cost of housing. (See Exhibit 18.)

For the $300–450 thousand price tier of housing, time costs are the largest component (See exhibit 19.) and add about 21% to the cost of housing. They are followed closely by fees, which add another 16%. The lack of an initial master plan for many projects developed in the City and a relatively long period involved in the mapping process are the primary drivers of time and financing expenses.

Requirements to provide affordable housing and land or units eliminated early in the entitlement process each add another 5% to the average price of housing.

Source: FBEI
San Marcos

Regulatory costs in the city of San Marcos typically represent about 27-29% of the cost of a new house. (See Exhibit 20.)

Exhibit 20

San Marcos Regulatory Costs

<table>
<thead>
<tr>
<th></th>
<th>0-300</th>
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<tr>
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<tr>
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<td>27.72%</td>
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<td></td>
</tr>
<tr>
<td>Total</td>
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<td></td>
<td></td>
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<td>27.58%</td>
<td>27.34%</td>
<td>27.72%</td>
</tr>
</tbody>
</table>

Source: FBEI

For the City of San Marcos, fees are typically the largest cost component, (See Exhibit 21.) but significant variation exists across different price segments. For the $300-450 thousand price tier of housing, fees account for about 12% of a new home’s price.

The fact that master plans are widely in place in the City helps contain time costs substantially. For the $300-450 thousand price range, time costs are about $19,000 per home, which is about one fourth of the expense in Carlsbad. However, this is still a sizable expense to be borne by home owners and renters at about 5% of the total cost of housing. The requirement to provide affordable housing adds another 6% to the average price of housing.

Exhibit 21

San Marcos Distribution of Regulatory Costs

Fees 45%

Affordable Housing 23%

Time Costs 19%

Entitlement Costs 4%

Other 9%

*$300-$450 Price Segment

Source: FBEI
Santee

Santee’s regulatory costs account for less than one-quarter of a home’s price, one of the lowest ratios in the region, albeit still a sizable number. (See Exhibit 22.)

Exhibit 22

<table>
<thead>
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<td>Cost % of Price</td>
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<td>21.52%</td>
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<td>Total</td>
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<tr>
<td>Total Weighted Price</td>
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<td>$289,900</td>
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<td>Total Weighted Regulatory Cost</td>
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<td>Cost % of Price</td>
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<td>21.52%</td>
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Source: FBEI

In Santee, fees account for about half of total regulatory costs in the $600 thousand and over price range where the largest share of sales took place in 2013. (See Exhibit 23.) They contribute approximately 10% to the average price in that segment. Time costs are the second largest element, accounting for about 8% of a home’s price in that bracket. The absence of an initial master plan for many projects in the City is a substantial factor raising the time and financing component. Other elements, including vertical costs, eliminated units, and mapping, each add 2% or less to the price of housing in the area.

Exhibit 23

<table>
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<td>45%</td>
</tr>
<tr>
<td>Eliminated Units</td>
</tr>
<tr>
<td>4%</td>
</tr>
<tr>
<td>Vertical Costs</td>
</tr>
<tr>
<td>6%</td>
</tr>
<tr>
<td>Time Costs</td>
</tr>
<tr>
<td>39%</td>
</tr>
<tr>
<td>Other</td>
</tr>
<tr>
<td>6%</td>
</tr>
</tbody>
</table>

*$600 -> Price Segment

Source: FBEI
Other Incorporated Cities

Regulatory costs in the other incorporated jurisdictions account for between 32% and 43% of the average price of a new home. (See Figure 24.)

Exhibit 24

Other Cities Regulatory Costs

<table>
<thead>
<tr>
<th></th>
<th>0-300</th>
<th>300-450</th>
<th>450-600</th>
<th>600-+</th>
</tr>
</thead>
<tbody>
<tr>
<td>Detached</td>
<td>Weighted Price</td>
<td>$394,514</td>
<td>$533,452</td>
<td>$821,617</td>
</tr>
<tr>
<td></td>
<td>Regulatory Cost</td>
<td>$148,826</td>
<td>$171,625</td>
<td>$311,995</td>
</tr>
<tr>
<td></td>
<td>Cost % of Price</td>
<td>37.72%</td>
<td>32.17%</td>
<td>37.97%</td>
</tr>
<tr>
<td>Attached</td>
<td>Weighted Price</td>
<td>$251,833</td>
<td>$355,546</td>
<td>$996,834</td>
</tr>
<tr>
<td></td>
<td>Regulatory Cost</td>
<td>$107,337</td>
<td>$144,600</td>
<td>$460,162</td>
</tr>
<tr>
<td></td>
<td>Cost % of Price</td>
<td>42.62%</td>
<td>40.67%</td>
<td>46.16%</td>
</tr>
<tr>
<td>Total</td>
<td>Total Weighted Price</td>
<td>$251,833</td>
<td>$365,174</td>
<td>$533,452</td>
</tr>
<tr>
<td></td>
<td>Total Weighted Regulatory Cost</td>
<td>$107,337</td>
<td>$145,644</td>
<td>$171,625</td>
</tr>
<tr>
<td></td>
<td>Cost % of Price</td>
<td>42.62%</td>
<td>39.88%</td>
<td>32.17%</td>
</tr>
</tbody>
</table>

Source: FBEI

Time costs and fees are typically the largest drivers of the regulatory component of home prices across most price tiers in many other cities located in San Diego County. In the $600 thousand price bracket (representing the largest share of 2013 sales) time costs add about 20% to the average home price. Fees trail at about 7%. (See Exhibit 25.)

Affordable housing requirements, initial set-asides resulting in a loss of potential units, and vertical costs also contribute to home prices in many jurisdictions.

Exhibit 25

Other Cities Distribution of Regulatory Costs*

<table>
<thead>
<tr>
<th>Component</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Time Costs</td>
<td>51.8%</td>
</tr>
<tr>
<td>Affordable Housing</td>
<td>12.2%</td>
</tr>
<tr>
<td>Eliminated Units</td>
<td>11.3%</td>
</tr>
<tr>
<td>Other</td>
<td>5.5%</td>
</tr>
<tr>
<td>Fees</td>
<td>19.2%</td>
</tr>
</tbody>
</table>

*$600-> Price Segment

Source: FBEI
In the unincorporated areas of San Diego County, regulatory costs increase the price of housing between around 20% and 30% depending on the price range. (See Exhibit 26.)

### Unincorporated Areas Regulatory Costs

<table>
<thead>
<tr>
<th></th>
<th>0-300</th>
<th>300-450</th>
<th>450-600</th>
<th>600-&gt;</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Detached</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Weighted Price</td>
<td>$442,990</td>
<td>$549,589</td>
<td>$989,319</td>
<td></td>
</tr>
<tr>
<td>Regulatory Cost</td>
<td>$92,271</td>
<td>$134,135</td>
<td>$305,428</td>
<td></td>
</tr>
<tr>
<td>Cost % of Price</td>
<td>20.83%</td>
<td>24.41%</td>
<td>30.87%</td>
<td></td>
</tr>
<tr>
<td><strong>Attached</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Weighted Price</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Regulatory Cost</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost % of Price</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>$442,990</td>
<td>$549,589</td>
<td>$989,319</td>
<td></td>
</tr>
<tr>
<td>Total Weighted Price</td>
<td>$92,271</td>
<td>$134,135</td>
<td>$305,428</td>
<td></td>
</tr>
<tr>
<td>Cost % of Price</td>
<td>20.83%</td>
<td>24.41%</td>
<td>30.87%</td>
<td></td>
</tr>
</tbody>
</table>

Source: FBEI

Fees and time or financing costs are the largest components of regulatory costs in the County’s unincorporated areas. (See Exhibit 27.) Despite the fact that most projects are built with a master plan already in place, the entitlement period is still typically a long 8-10 years in most areas. The period for securing mapping approvals is also relatively long in unincorporated areas under the jurisdiction of the County.

For the $600 thousand and up price bracket, time costs amount to about 20% of the average home price in unincorporated areas, fees follow at approximately 5%. Units lost to requirements for more vacant space or other uses represent the third largest component at about 4% of a home’s price.
V. THE ECONOMIC BENEFITS OF REGULATORY REFORM ON HOUSING ACCESS

Approximately 58% of households in the total County of San Diego can afford to buy or rent a new home in the region based on current levels of income and the levels and structure of home prices in the region. As noted above, the options available to others include using accumulated assets; relying on the financial assistance of family members or friends; living with relatives, friends, or acquaintances; finding housing in the existing stock of units; or leaving the region to find less expensive housing elsewhere.

The analysis of this study shows that without the various costs of housing regulations, approximately 79% of households around the region could afford the average priced home. The “gap” is significant at 21% or approximately 233,000 households. (See Exhibit 28.)

It would be futile to argue that regulatory costs could be slashed to zero or even cut in a major way immediately. The economy does not even possess the capacity to suddenly ramp up the production of homes on a massive scale. In 2014, an estimated 9,000 building permits for new housing units are expected to be issued. Even during the boom housing years of the late 1980s, the maximum number of housing permits issued was about 44,000 in 1986.

However, a more gradual approach would appear to be politically, socially, and economically feasible. If average regulatory costs could be pared about 3.0%, an additional 6,749 of the households priced out of the market could financially qualify for the new housing market in one year.
Would the regulatory cost savings be passed on to consumers or retained by developers? While some temporary boost in profits might occur, competition and the increase in housing supply would push the savings to homebuyers in the form of lower housing costs. Some have argued that regulatory costs are not borne at all by consumers but instead lead to a reduction in the price that developers are willing to pay for raw land. This, however, can cause land to be diverted to other uses or held for the future. The subsequent reduction in the supply of residential land and housing units means higher costs to the consumer. Any reduction in regulatory expense would yield tangible benefits for potential homebuyers.

The elasticity or impact of regulatory reduction is nearly 1:1 with the current structure of home prices and income distribution. A three percent reduction in average housing costs should generate a nearly equal gain (2.9%) in households able to purchase or rent housing. These households would be accommodated with a companion expansion in homebuilding activity.

The annual economic benefits would be large. (See Exhibit 29.) San Diego County’s total economy could see a rise in its gross regional product (GRP) of $3.1 billion or 1.7%. This reflects not only the direct impact of increased construction activity but also the ripple or multiplier effects as those additional building dollars flow through the economy. Purchases all along the various supply chains and the additional consumer spending that takes place due to more jobs and pay feed the ripple impacts.

The region’s total personal income would see a boost of $2.5 billion or 1.5% while employment would experience a gain of approximately 37,000 jobs. A large increase in construction workers would take place along with gains in positions in engineering, architecture, and real estate. The ripple effects would generate job gains in other areas of the economy, including retailing, wholesale trade, financial services, and health care. Along with the increases in economic activity, an addition of nearly 1,400 new businesses would be projected to be established.

### Exhibit 29
**Economic Impact of 3% Average Reduction in Regulatory Costs**

<table>
<thead>
<tr>
<th>Component</th>
<th>Increase</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross Regional Product, $ bil</td>
<td>$3.15</td>
<td>1.7%</td>
</tr>
<tr>
<td>Personal Income, $ bil</td>
<td>$2.54</td>
<td>1.5%</td>
</tr>
<tr>
<td>Employment</td>
<td>37,331</td>
<td>1.9%</td>
</tr>
<tr>
<td>Business Enterprises</td>
<td>1,372</td>
<td>1.7%</td>
</tr>
<tr>
<td>Population</td>
<td>18,222</td>
<td>0.6%</td>
</tr>
<tr>
<td>Housing Permits</td>
<td>6,749</td>
<td>75%</td>
</tr>
</tbody>
</table>

Source: FBEI
The expected 6,750 increase in building permits to a total of about 16,000 units would represent a jump of about 75% from the 9,000 level estimated for 2014 and put the total at the best level since 2004.

San Diego County’s total population could be expected to be about 18,000, or 0.6%, greater than would otherwise exist. During the last three years, net domestic outmigration has averaged about 11,000 per year. Lower housing prices could shift that number to a net inflow of approximately 7,000 residents per year. In 2001, net domestic immigration (from other parts of California and other states) equaled about 2,500, and in 1999 it exceeded 15,000.

All of the various cities and unincorporated areas would reap significant economic gains from reduced regulatory costs. (See Exhibit 30.) Allocating them in proportion to their share of the County’s total households demonstrates the widespread benefits of regulatory reform even on a relatively modest scale.

<table>
<thead>
<tr>
<th></th>
<th>Carlsbad</th>
<th>Chula Vista</th>
<th>San Diego City</th>
<th>San Marcos</th>
<th>Santee</th>
<th>Other Cities</th>
<th>Unincorporated Areas</th>
<th>Total San Diego County</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross Regional Product, $ mil</td>
<td>$121</td>
<td>$223</td>
<td>$1,395</td>
<td>$82</td>
<td>$56</td>
<td>$462</td>
<td>$807</td>
<td>$3,147</td>
</tr>
<tr>
<td>Personal Income, $ mil</td>
<td>$98</td>
<td>$179</td>
<td>$1,124</td>
<td>$66</td>
<td>$45</td>
<td>$373</td>
<td>$651</td>
<td>$2,536</td>
</tr>
<tr>
<td>Employment</td>
<td>1,440</td>
<td>2,641</td>
<td>16,548</td>
<td>969</td>
<td>669</td>
<td>5,486</td>
<td>9,577</td>
<td>37,331</td>
</tr>
<tr>
<td>Business Enterprises</td>
<td>53</td>
<td>97</td>
<td>608</td>
<td>36</td>
<td>25</td>
<td>202</td>
<td>352</td>
<td>1,372</td>
</tr>
<tr>
<td>Population</td>
<td>703</td>
<td>1,289</td>
<td>8,077</td>
<td>473</td>
<td>327</td>
<td>2,678</td>
<td>4,675</td>
<td>18,222</td>
</tr>
<tr>
<td>Housing Permits</td>
<td>260</td>
<td>477</td>
<td>2,992</td>
<td>175</td>
<td>121</td>
<td>992</td>
<td>1,731</td>
<td>6,749</td>
</tr>
</tbody>
</table>

Source: FBEI

Reducing the number of households priced out of the market by various regulations by about 3% clearly makes only a small dent. Nevertheless, an annual increase of about 6,700 households into the market over the course of 15 years would close over forty percent of the current gap.

This analysis demonstrates the major economic benefits of easing the regulatory burden only modestly or at the margin. It also shows the economic costs of failing to address the issue.
VI. LAND SUPPLY AND DEMAND

Land Supply

One of the major factors contributing to the high cost of housing in San Diego County is the availability, or lack thereof, of suitable land inventory on which homes can be built. San Diego County encompasses 2.7 million acres of land. It is bordered by Camp Pendleton to the north, Mexico to the south, the Pacific Ocean to the west, and mountains to the east.

Currently, less than 16% of the County’s total acreage is considered “developed.” Most of the developed land is situated along the coastline and extends some 20 miles inland. The vast majority of acreage in the County (72%) is considered “undevelopable.” The reasons for this are several: much of the undevelopable land has mountainous terrain, it is subject to steep slope development regulations, and there is a lack of appropriate infrastructure. These reasons combine to leave the majority of this acreage non-accessible to development.

Within this “undevelopable” designation, there is significant acreage that is geographically suitable for development, but which has been designated as open space and/or open space preserve. San Diego County, as a whole enjoys, one of the most robust open space preserve systems in the country. Through the City’s and the County’s “MSCP” multiply species conservation plans (MSCPs) and Habitat management plans (HMPs), tens of thousands of acres have been set aside to preserve open space and wildlife. Much of this acreage is adjacent to developed land and would be suitable for development without this preserve designation.

While fulfilling valuable public objectives, this reduction in available land inventory has clearly had an inflationary effect on the cost of raw land as population and housing demand have continued to climb.

Housing Demand

According to the San Diego Association of Governments (SANDAG) 2010 Regional Growth Forecast, the household population in San Diego County will continue to rise to 4.2 million residents by 2050. This growth will create the need for an additional 400,000 housing units by 2050. This represents an additional 11,000 housing units each year for the next 36 years.

With the inability to look outward for land inventory, much of San Diego’s housing needs will have to be met looking inward. This means infill locations and redevelopment of existing neighborhoods. This densification of developed areas will change the character of housing stock in San Diego, moving away from traditional detached suburban homes to infill attached product.
Although, this new paradigm will not be growth outward, cost are expected to remain high as opportunities for this type of growth are difficult, often finding their own unique obstacles such as infrastructure deficits and neighborhood opposition.

With growth prospects for the region high and availability of suitable building sites low, it is inevitable that prices will continue to increase for housing in San Diego for the foreseeable future.
Traditionally, developers and homebuilders have been on a collision course with public officials charged with implementing housing policies. The public has been caught in the crosshairs and high home prices and rents have been the result.

This report calls for a new collaborative approach, which has historically been one of San Diego’s core strengths in the case of biotech and many of the other drivers of our economy. Improvements at the margin in the regulatory process could yield benefits to all those involved.

Our research concludes that improvements or standardization in key areas of the home building process could assist to achieve the objectives of the public and policy officials, but at a significantly lower cost.

**Best Practices**

Extensive interviews with builders and developers throughout the region revealed elements of "best practices". Our research team has incorporated those elements and other information obtained from each jurisdiction to establish a broader set of best practices, those methods, practices, or processes that consistently deliver superior results. Additionally, best practices seek to use approaches and methods that minimize resources, refine an approach, and foster sustainability.

Information sharing and collaboration across jurisdictions will allow for the development of a standardized approach to best practices and a "win-win" for builders, developers, and customers by allowing for efficiencies throughout all of the phases of the home building process to improve the end result. Our hope is that these best practices will be a model for the future and will be utilized by not only the jurisdictions that we studied, but other jurisdictions in the region, and perhaps throughout the country.

- Expedite the turn around time and approvals for permits by creating a clear process and centralized location for information.

- Have a master plan in place to streamline the entire entitlement process to reduce political and litigation risks, and shrink time and financing costs.

- Develop a review process in each jurisdiction to foster accountability and ensure that policy and procedures established are being adhered to. This process should follow basic management principles.

- Encourage cross-jurisdiction collaboration to share information and ideas to continue to refine and enhance efficiency in the process.
Implement a “No Late Hits” policy in the building approval process to prevent additional comments and challenges to be submitted after the map or final project has been approved.

Establish uniform codes for road and green building across all jurisdictions, similar to practices in Santa Clara County.

Standardize Title 24 requirements across the life of each development.

The Entitlement Process

Because of the long duration of the entitlement phase (3 to 10+ years) and the high cost of financing in this phase of a housing project (typically 18%), several regulatory improvements could have a substantial impact on lowering home prices.

The compensation/incentive system governing city employees working in planning and development departments should be revamped from the current structure that implicitly rewards them for taking more time to process and approve plans. Benchmarks on approval times should be set and used in awarding bonuses for beating those benchmarks while checks for quality are carefully made.

Once a master plan is approved, no more changes should be allowed. Reopening the process often results in new inspectors starting the process over again from the beginning.

Jurisdictions should move forward to create master plans in order to expedite the development of future projects.

Once the EIR has been approved, individuals or groups opposing it should be required to pay some of the costs associated with the opposition process. This could include a bond for the legal costs involved.

Best practices should be studied in Arizona, Colorado, and Texas, where residential properties are being developed more quickly and efficiently.

Litigation should be limited to the early stage of the development or building process. Legal challenges should only be allowed until the tentative or final map is approved. No further litigation should be allowed after that point on issues unless major revisions are made to the original plan.
• Efforts should be made to seek CEQA and tort reform in a way that balances costs versus benefits.

**Mapping**

The mapping process typically involves substantial redundancies and delays in securing a project’s approval. Several changes could be positive on a cost benefit basis.

• Allow all phases of the project to be grandfathered under the originally approved plan. This would prevent extended and costly reviews of elements previously endorsed.

• Mapping is completed by consultants and engineers who are licensed and warranted for the quality and precision of their work. They should be able to certify the quality of their work, avoiding the necessity of detailed reviews.

• Current practice is that cities conduct their own review process, with a full cost recovery of the time and staffing resources required to be paid by the builder/developer. This system should be replaced by a flat fee or fixed cost.

• A 30-day review process should be required and, if not met, result in compensation paid by the jurisdiction. Third party licensed architects should be allowed to conduct the review process. These reviewers or third parties should be able to communicate with the developer/builder to obtain key information or data.

• No additional comments should be allowed after the review process is completed. A “No Late Hits” policy should be implemented, with minor issues prohibited from causing project delays. Major issues should be elevated to senior government officials for resolution.

Various regulatory costs and delays in the process of developing raw land, securing the necessary permits for construction, and building the house can add substantially to the price of a home. Several recommendations could help reduce this cost.
Land Development and Building

- Standardize building codes for all jurisdictions within the County of San Diego. For example, standardizing road building codes could reduce inefficiencies and costs for developers.

- Fee credits should be given to partially offset the cost of public parks, trails, or facilities that may be mandated. Such credits should not trigger prevailing wage laws.

- Establish benchmarks for the processing and approval of permits. Publish data on the performance of different jurisdictions.

- Establish “one-stop” shops for all permits that must be secured for a housing project.

- Standardize Title 24 requirements across the various build-out phases of a development. This would avoid making it necessary for each phase to move through another review process.

- Repeal Section 112.0310 of the San Diego Municipal Code that allows unlimited appeals and public hearings on issues related to CEQA after the project has been approved and determined to be consistent with CEQA requirements. These appeals and hearings can delay projects for long periods of time and add substantially to costs even after CEQA standards have been achieved or exceeded.

Affordable Housing

Local efforts to provide more affordable housing could be improved to mitigate the impact on individuals and households who do not qualify for such accommodations.

- An in-lieu fee should be available as an alternative to building affordable housing units, especially for small projects.

- A sliding scale for affordable housing would help builders and developers who typically have economies of scale. Requiring 10% or more of small projects’ units to be affordable can be inefficient and costly.

- Incentives or expedited processing of building proposals should be given to projects exceeding affordable housing requirements.
• California’s Density Bonus Law allows developers to obtain more favorable local development requirements (ranging from allowing higher densities to reduced parking requirements.) Allow inclusionary and density bonus units to be built off site from the project that generates the requirement. Carlsbad allows this as long as the affordable units are built in the same quadrant of the city where the market rate housing is located.

• Allow inclusionary and density bonus units to be aggregated with other affordable units to achieve economies of scale.

• Create an affordable housing bank where market rate developers can “purchase” affordable units. Carlsbad allows this and it works well.

• Contribute or sell on favorable terms land that is owned by a city and is suitable for affordable housing. Accept payment out of the net cash flow from the project.

The above are intended to be illustrative of improvements to the regulatory process that could be made, yielding large dividends in terms of lower housing costs. The system is currently broken. A dialog and collaboration involving builders /developers and public officials should take place to find new and better systems for meeting the public’s demands for safety, quality of life, and environmental integrity at a reasonable price.
This study involved three major modules:

- Data collection and estimation of all the dimensions of regulatory costs for the seven different jurisdictions in different price segments, for single-family and multi-family units, within those jurisdictions

- Development of a model to estimate the households priced out of the market in different segments and jurisdictions by housing regulations

- Estimation of the economic benefits that could accrue to the overall region and its constituencies of reducing the impact of regulation

The analysis covered seven jurisdictions in San Diego County: Carlsbad, Chula Vista, the City of San Diego, San Marcos, Santee, other incorporated cities as a group, and unincorporated areas in San Diego County. The overall market was divided in four price tiers:

- $0-300k
- $300-450k
- $450-600k
- $600k +

Both single-family and multi-family housing markets were investigated. Extensive and comprehensive data on total sales of new housing units, new rental units absorbed, square footage, prices, and rents for all of these segments was secured for 2013. Price equivalents for rents were calculated using a standard model determining the monthly and annual payments that would be required under current conventional mortgage terms and interest rates, insurance premiums, and local tax rates. The home prices consistent with the monthly and annual housing payments equal to the rental costs were then calculated.

### Regulatory Costs

Data or estimates of seven different components of regulatory costs were secured: entitlement, mapping, fees, eliminated units, vertical costs, affordable housing, and time.
Entitlement, Mapping, and Fees

When calculating entitlement and mapping costs, estimates were based on professional opinions from the interviews with builders and developers active in various market geographies in the different areas of San Diego County. For entitlement costs, a typical expense is approximately $9,000 per unit per year over a three year period. Half of that cost ($4,500) goes towards regulation. For mapping costs, which usually span an 18-month period, a typical expense is approximately $9,000 per unit. About $5,000 per unit represents the fee paid to private consultants to create the project plan (maps, grading plans, and improvement plans). The regulatory cost component is about $4,000 per unit and represents the expense of reviewing and approving the mapping documents.

Fee data was based on an extensive collection of information from the builders and developers from the various jurisdictions. All fees were included, such as fees for drainage, sewer connection, water, schools, traffic, building permits, and other dimensions.

Once the data was categorized according to type of cost, a reality test was conducted to observe “cost behavior.” This was completed by first standardizing all values to make them comparable and then looking at cost as a percent of price. Once these ratios were calculated within the given price segments across all six cities explicitly studied, they were averaged and the standard deviation was studied.

All categories within the cost pool had a standard deviation less than 3.5% (most price segment categories had a standard deviation less than 1%) and thus these cost structures across all jurisdictions seem relatively stable.

Once cost to price ratios were calculated and analyzed for variation, cost projections were estimated for the other incorporated cities jurisdiction. Estimates were calculated by multiplying the average cost to price ratio across jurisdictions to the total weighted price in the corresponding price segment. These costs are accounted for under the category entitled “Fees.”
Elimination of Units

The elimination of units methodology began with the weighted average sales price and number of units sold for each price segment and jurisdiction. The number of units sold was divided by 1 minus the percent of eliminated units for each jurisdiction, arriving at the total number of potential units. The percent of eliminated units per jurisdiction was obtained during meetings between the FBEI and builders / developers in the city.

The number of actual units sold was subtracted from the potential units to arrive at the number of units eliminated. To determine the price at which to value the units eliminated, the average sales price for each price segment was multiplied by the finished lot to home price ratio to obtain the finished lot price. Both sales prices and finished-lot-to-home price ratio data were obtained from the builders and developers in the County. The finished lot price was then reduced by the total fees and estimated cost for mapping and entitlements obtained from the builders and developers in the county to obtain an estimate of land values. Downward adjustments to average fixed costs were made where negative land values were observed.

The estimated value of eliminated units was then divided by the actual number of units sold to arrive at the average cost of lost units across each price segment for each jurisdiction. The reasonableness of the estimates was checked by examining the ratio to average home prices.

Vertical Costs

The first step in the process was to determine the mean vertical cost per square foot across the County. Using the responses from questionnaires and subsequent interviews with major builders and developers, a spreadsheet was created to summarize the data. Some builders and developers had provided vertical cost data with per unit values and others had responded with per square foot values. Many survey respondents had also given a range of values, as opposed to just one single estimate of vertical costs.

Using the County-wide average for new homes of 2,550 square feet, the respondents’ data that had been provided per square foot was converted to per unit data. For those respondents who had given a data range, low and high values were noted in separate columns. Once all data was stated on a per unit basis, the mean of the low and high value columns were each determined. These means were converted back to a per square foot value, and then the mean between the low and high values was calculated to arrive at the overall mean vertical cost per square foot of $2.65.
Once the mean vertical cost had been determined, a new spreadsheet was created. A table was then created for each jurisdiction and for each of the four housing price ranges within those jurisdictions by housing type (detached or attached), noting the average square footage for each and multiplying that value by $2.65 per square foot to arrive at the vertical cost per unit for each jurisdiction/housing type/price range possibility.

As a check for reasonableness, on the same spreadsheet, a table was created containing the weighted average house price for each jurisdiction/housing type/price range. A third table was then created to calculate the vertical cost as a percentage of the weighted average house price for each possibility. In virtually all cases, the vertical cost to housing price ratio was approximately 1%.

**Affordable Housing**

The methodology used to obtain the cost associated with the affordable housing mandate began with the finished lot price for each price segment and jurisdiction. This was obtained by multiplying the weighted average sales price by the finished-lot-to-home price ratio for each segment and jurisdiction. Both the weighted average sales price and the finished lot to home price ratio data were obtained from the builders and developers.

The number of units sold for each price segment, also data obtained from the builders and developers, was divided by 1 minus the affordable housing requirement for that municipality (generally 10%-15%), yielding the total number of units possible if no mandate was in place. The potential units were reduced by the actual to arrive at the number of units eliminated.

To spread the cost of the land across the actual units, the price of the finished lot was multiplied by the number of units eliminated and then divided by the number of actual units sold. To see the impact of this cost, the fee was divided by the weighted average sales price for each segment in each jurisdiction.

A requirement of 10% was utilized for the other incorporated cities that were not individually included in the study.
Time Costs

The time cost calculation involved multiple steps. The first main step was to determine the average length of time it takes a builder/developer to complete each phase of the project (entitlements, mapping, infrastructure development, permit review, and building) for each jurisdiction, with and without a master plan, and the average cost of funds at each stage. This information was obtained from meetings that FBEI had with builders and developers. Fixed and variable costs for each phase were also obtained in this manner.

The next primary step involved creating a spreadsheet that summarized the general flow of funds at each phase and applying the appropriate cost of funds and length of the phase to determine the capital cost during that phase. Total capital cost was then determined by summing the results from the five phases (significant overlap of phases was assumed). The base case assumed that the land development phase overlapped both the mapping and permit review stages, resulting in only four distinct time periods. These calculations were made twice for each jurisdiction (once assuming that there was a master plan and once assuming that there was no master plan) by price range and by designation of attached or detached unit. In the cases where negative land values resulted, due to the preceding downturn in the real estate market, fixed costs were adjusted downward.

The final essential step in the process was to determine the weighted average cost of capital based upon the percentage of homes sold with a master plan in place and the percentage that had no master plan, for each jurisdiction by price range and attached or detached. The data on home sales of master plan versus no master plan was obtained directly from builders and developers based on building and sales activity for 2013. The resulting weighted average cost of capital for each case was then divided by the average home price in that case to ensure consistency.

Housing Impact Model

The model used to calculate the numbers of households priced out of different market segments in each jurisdiction was based partly on the methodology employed by the California Association of Real Estate in its calculation of its Housing Affordability Index (HAI).

For each price segment in each jurisdiction, the average income necessary to support the monthly and annual payments was used for the average priced home in that tier. Since the choice between ownership and renting is primarily a financial decision, no distinction was made in terms of the type of ownership.
The required downpayment was assumed to be 20%. Monthly payments and their annual equivalent were calculated for the sum of principal, interest, taxes, and insurance. Property tax rates as the different jurisdictions were obtained from the San Diego County Assessor’s Office. Mortgage interest rates were obtained from the latest readings from the Federal Housing Finance Board based on a composite of fixed and adjustable rate mortgages. A 30-year term was assumed. Monthly insurance payments were assumed to be .38 percent of the home price divided by 12. It was assumed that the monthly interest payment cannot exceed 30% of a household’s income in order for the prospective buyer to qualify for a loan.

The income distributions of households in each jurisdiction were obtained from the U.S. Census Bureau and SANDAG and converted into current dollars by FBEI. Calculations were then made as to the number of households who could uniquely qualify for a particular price segment of the housing market (could not afford higher prices and did not have to go lower). The sum was used as an estimate of the total share and number of households who could afford housing in each jurisdiction of these segments.

Calculations were then made in the same matter but with prices excluding the effect of regulations in each segment. The differences were then calculated to indicate the share and number of households priced out of housing in each jurisdiction by housing regulations.

**Economic Impact**

The economic benefits of regulatory reform were based on an analysis of a 3% reduction in the weighted average cost of regulation in each of the four housing price tiers for the total San Diego region. This percentage was based on an analysis of what the region’s homebuilding industry could reasonably accommodate and also by examining what might be reasonable in-migration patterns.

An estimate of the increase in sales was then based on the number of additional housing units that could be produced multiplied by the average price. The price used was net of the reduction in regulatory costs. This data was input into the IMPLAN© Model to trace through all of the direct and indirect economic effects. IMPLAN© is a widely used tool to conduct economic impact analysis.

Estimates of the impact on real GRP, personal income, and employment were secured. Implicit multipliers were analyzed for accuracy. The number of additional business establishments was estimated based on an analysis of the relationships between GRP, firm numbers, and population counts over time and in different areas. The relation between GRP and business establishments for San Diego was used as the final base for estimation.
Population estimates were based on the latest ratios of the number of individuals per household for different jurisdictions provided by the California Department of Finance, Demographic Research Unit.

Data, calculations, estimates, and results were checked throughout the process of the study to insure accuracy and consistency.
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The California Homebuilding Foundation invests in the future of homebuilding through: Endowments that provide scholarships and fund industry research; publishing current construction and new home statistics; presenting training seminars; and supporting high school courses that encourage young people to choose careers in the industry.