



Housing Innovation in Arizona:

Opening the Door to Arizona's
Housing Future

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ABOUT THE AUTHORS

2022 CSI Arizona Housing Fellows Sean Bowie and Jenn Daniels are CSI Arizona's first fellowship partners and both have a long history of policymaking and expertise in housing.

Senator Sean Bowie represents Legislative District 18, which includes Ahwatukee, west Chandler, southwest Mesa, and south Tempe. Sean is serving his third term, after first winning office in November 2016 and winning re-election in November 2018 and November 2020. After not seeking re-election his current term ends in January, 2023. In addition to his work at the Senate, Sean also works as a Professor of Practice at ASU's School of Public Affairs, where he teaches courses on leadership, ethics, and research methods.

Jenn Daniels has been an elected leader for over a decade, serving as a Council Member, Vice-Mayor and the Mayor of Gilbert, Arizona. She also currently serves on the Women United Steering Committee and sits on the Board of the Arizona Commerce Authority. Jenn's experience spans a broad spectrum that encompasses both her public and private expertise.

TEAMS & FELLOWS STATEMENT

CSI is committed to independent, in-depth research that examines the impacts of policies, initiatives, and proposed laws so that Arizonans are educated and informed on issues impacting their lives. CSI's commitment to institutional independence is rooted in the individual independence of our researchers, economists, and fellows.

At the core of CSI's mission is a belief in the power of the free enterprise system. Our work explores ideas that protect and promote jobs and the economy, and the CSI team and fellows take part in this pursuit with academic freedom. Our team's work is driven by data-driven research and evidence. The views and opinions of the team and fellows do not reflect institutional views of CSI. CSI operates independently of any political party and does not take positions.

ABOUT COMMON SENSE INSTITUTE

Common Sense Institute is a non-partisan research organization dedicated to the protection and promotion of Colorado's economy. CSI is at the forefront of important discussions concerning the future of free enterprise in Arizona and aims to have an impact on the issues that matter most to Arizonans.

CSI's mission is to examine the fiscal impacts of policies, initiatives, and proposed laws so that Arizonans are educated and informed on issues impacting their lives. CSI employs rigorous research techniques and dynamic modeling to evaluate the potential impact of these measures on the Arizona economy and individual opportunity.

Common Sense Institute was founded in 2010 in Colorado originally as Common Sense Policy Roundtable. CSI's founders were a concerned group of business and community leaders who observed that divisive partisanship was overwhelming policymaking and believed that sound economic analysis could help Coloradans make fact-based and common sense decisions.

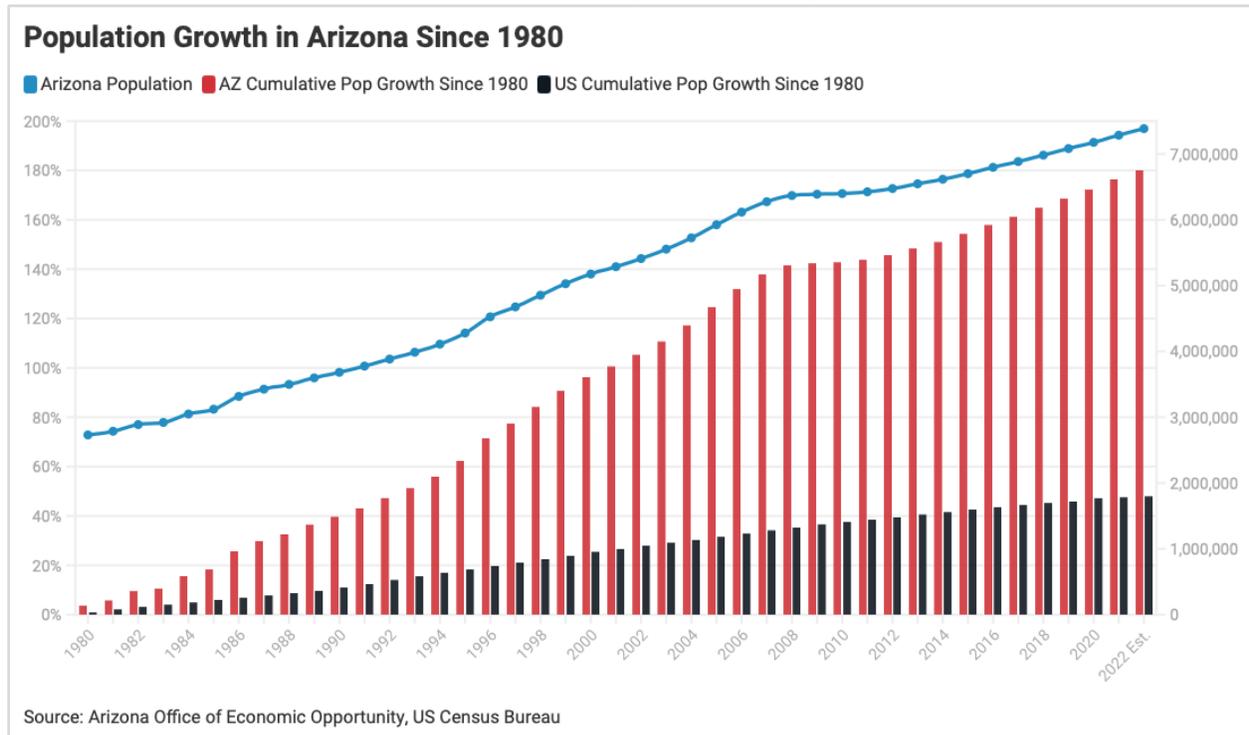
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INTRODUCTION

Few states have grown as rapidly in recent decades as Arizona. The state's premier quality of life, historically low cost of living, mild climate, low regulatory environment, and simplified tax structure will continue to draw people and businesses from other states for decades to come.

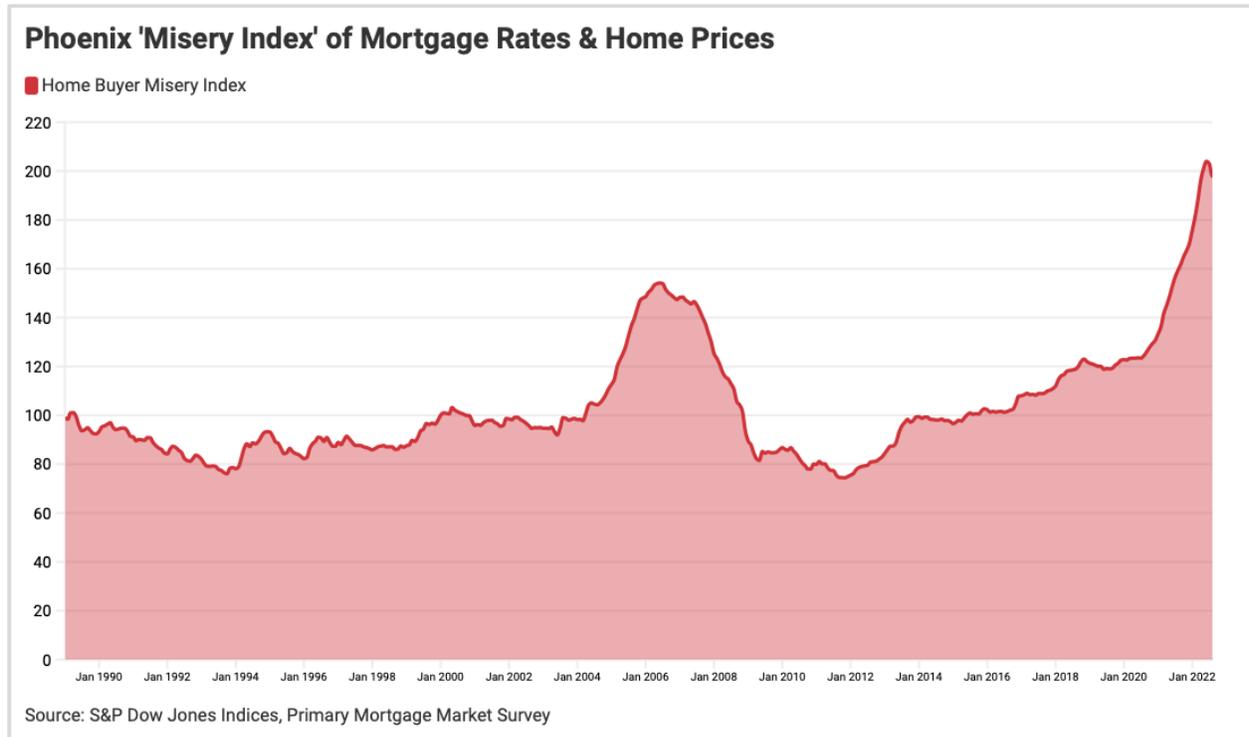
These factors have led to record population growth in recent years, with over 7.4 million residents now calling Arizona home. The COVID-19 pandemic, in particular, drew new residents to the state, as remote work allowed Americans to live and work anywhere they chose.



Keeping up with this population growth has been a challenge; Arizona does not have enough housing units to meet current and anticipated demand. While measuring this shortfall is necessarily a subjective exercise and estimates vary, several sources – including an October [CSI report](#) – put the estimate in the neighborhood of 100,000 unitsⁱⁱⁱ. The reasons for this are myriad and represent economic, political, and regulatory hurdles that have limited the amount of housing supply approved and built-in recent years, leading to rapidly rising housing and rental costs for residents. As a consequence, the Phoenix Homebuyers Misery Index shows conditions today for homebuyers to be worse than ever, and the period of historically low mortgage interest rates that buoyed the state's and the nation's inflated home prices appear to be at an end. The Misery Index, as developed by Common Sense Institute Arizona, sums normalized and equally weighted home prices and 30-year mortgage rates to measure effective costs of

homebuying relative to historical levels. The index is set to a value of 100 in January, 2000 and has risen to 203 in 2022.

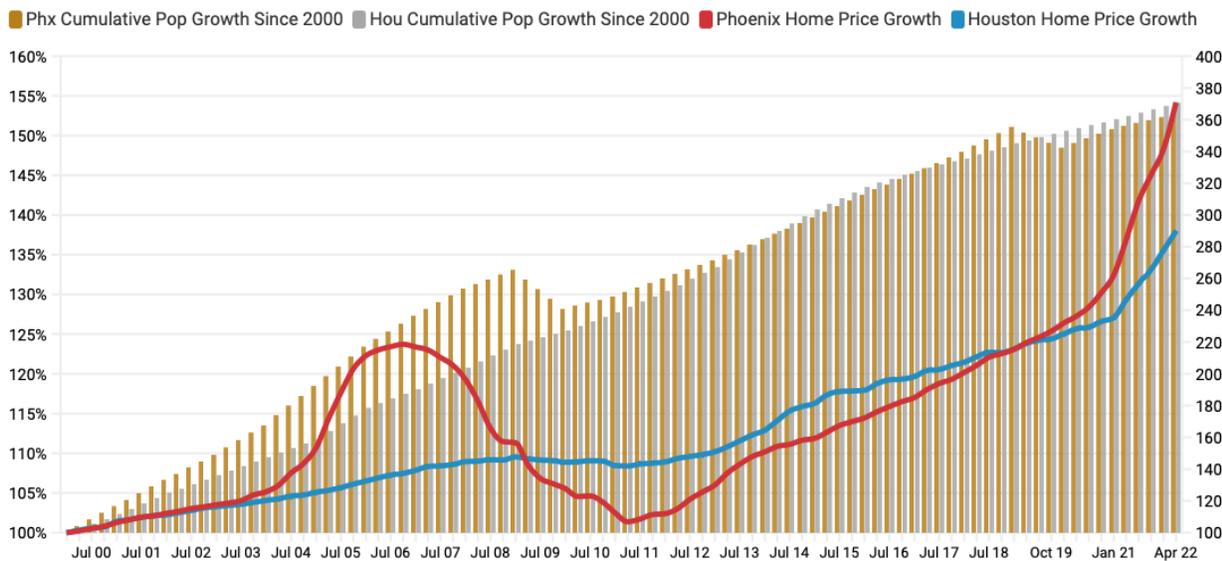
Decades of outward suburban growth have limited the amount of land available for development, particularly in Maricopa County. Community



opposition to development, and increased density in particular, has led to longer approval periods and projects being sidelined due to political pressure on local officials. Barriers to development at the state level, and bureaucracy within state agencies, have limited the options available to local governments to approve more units, particularly affordable housing. And often unnecessary and burdensome rules and regulations by local governments have delayed project start times and increased costs for developers and homebuilders.

Population & Home Price Growth in Phoenix, AZ & Houston, TX

Despite exhibiting similar population growth trends, home prices in the Phoenix market have exhibited more volatility since 2000 than in the Houston area



Source: US Federal Housing Finance Agency, US Census Bureau

This failure to approve and build enough housing supply has led to several deleterious effects that have rippled across our state's economy.

Infamously, Houston, TX – a city of comparable size to Phoenix and that has seen nearly the same cumulative population growth since 2000 – has no formal local zoning classification rules. Also strikingly, the city has experienced far less home price volatility than our fastest growing metro area. The city experienced average home price growth during the 2004-2006 period, and no significant price declines during or after the Great Recession. Appreciation during the current cycle is roughly in-line with national average price growth, and about half the rate of price growth seen in the Phoenix metro market since 2020. According to the US Census Bureauⁱⁱⁱ, between 2010 and 2020 the Houston metropolitan area added over 400,000 housing units and increased its housing supply by nearly 20%.

Arizona, on the other hand, has complex local zoning classification rules, and the process for changing them can be onerous and lengthy, particularly in many of the Phoenix metro area's jurisdictions. Over the same time period the Phoenix metro area added only about 200,000 units and increased its housing supply by just over 10%.

The Houston result is not the norm; the Phoenix experience since the end of the Great Recession is typical. A 2018 paper by Aastveit et. Al. found that, across 254 studied U.S. metro areas, housing supply elasticities were significantly lower today than during the mid-2000's^{iv}. Meaning that supply

was less sensitive to rapid price appreciation during this cycle than the prior, and prices rose faster than they would have otherwise. The causes of the decline in permits are likely attributable to some combination of:

- Areas readily available for residential development were likely already built out during the previous expansionary period.
- Regulatory standards, including, for example, financial and lending standards were tightened during and after the Great Recession in response to the widespread belief that speculative overbuilding contributed to that crisis.
- The increasingly stringent zoning, environmental, and building codes and standards that made it more expensive and time-consuming to build a home.



Neighborhood in Houston, TX featuring adjacent single- and multi-family housing.

A 2003 National Bureau of Economic Research study of major American cities estimated that residential land-use restrictions – including zoning codes – raised home prices by “at least” 10% (and by up to 50% in jurisdictions like Manhattan)⁹.

Simply put, Arizona has a housing crisis and needs more housing. Resolving it will require more than just tinkering around the edges of public policy. Thoughtful, bold, and swift action is required.

Our report outlines over a dozen policy recommendations that state lawmakers and local elected leaders should consider and introduce when the 56th Arizona legislature convenes in January and as soon as allowable on the local front. These recommendations represent bipartisan consensus on the best path forward, and stem from dozens of conversations we have conducted this year with stakeholders across the housing spectrum.

Resolving our housing crisis will require an “all-of-the above” approach consisting of streamlined rules and regulations on zoning and permitting decisions, eliminating several state pre-emption policies to remove barriers to more development, greater use of state resources to encourage and incentivize local governments to approve more construction, and an investment in our workforce pipeline.

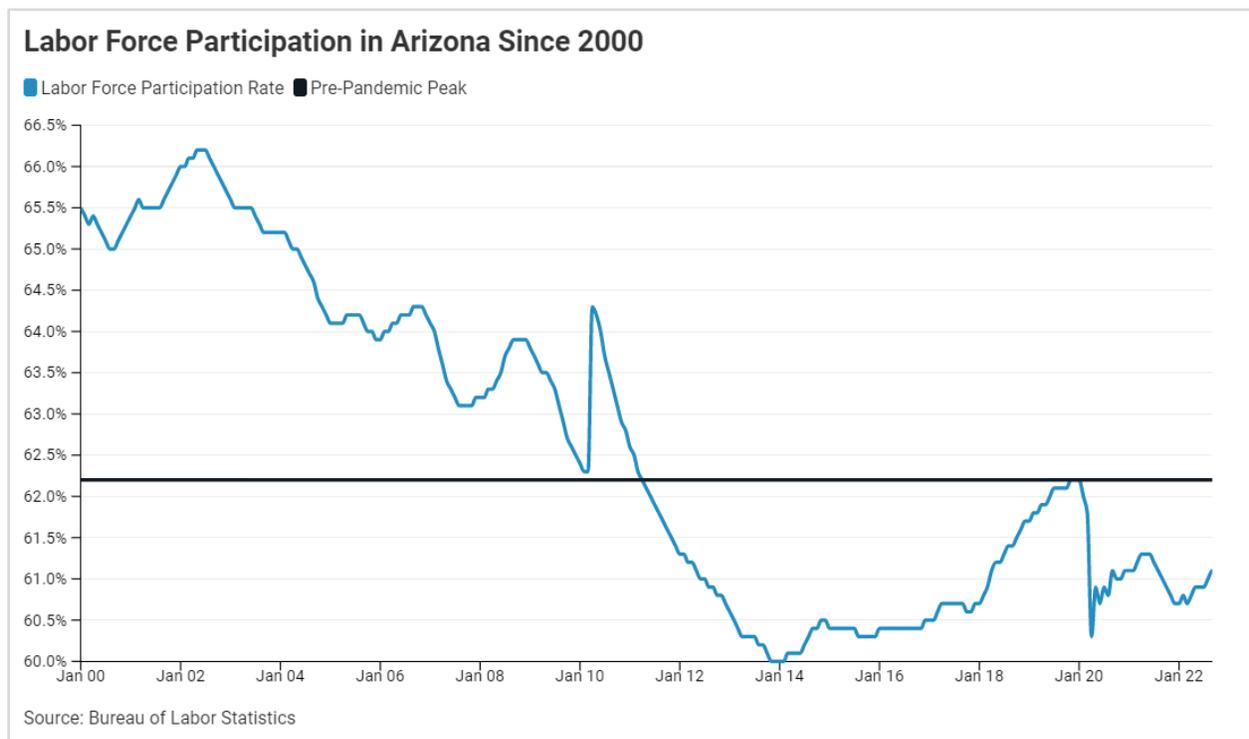
This multi-pronged approach addresses every level of the housing cycle, from home builders to local governments to the Arizona Legislature. It

requires greater accountability for each and incentivizes actions to increase housing supply statewide.

Most policy decisions around zoning and development occur at the local level, and often require years-long processes and approvals before shovels can hit the ground. There is no doubt, local laws and ordinances restricting growth or unnecessarily slowing or stopping development must be either justified or removed entirely from law.

Additionally, for local governments that are working to solve this problem and approving more units to meet demand, they lack several key policy tools that could be useful to get more housing supply online and available for its residents, particularly affordable housing. In some cases, they lack these tools due to statewide pre-emption laws put into place by the Arizona Legislature in recent years, limiting their flexibility and ability to innovate at a time when multiple policy levers are needed to better respond to this crisis.

Removing specific statewide pre-emption policies that restrict local governments from approving more development will eliminate barriers for local decision making and place greater accountability on these cities and towns to get more housing approved and online quickly. With these reforms, there should be no excuses.



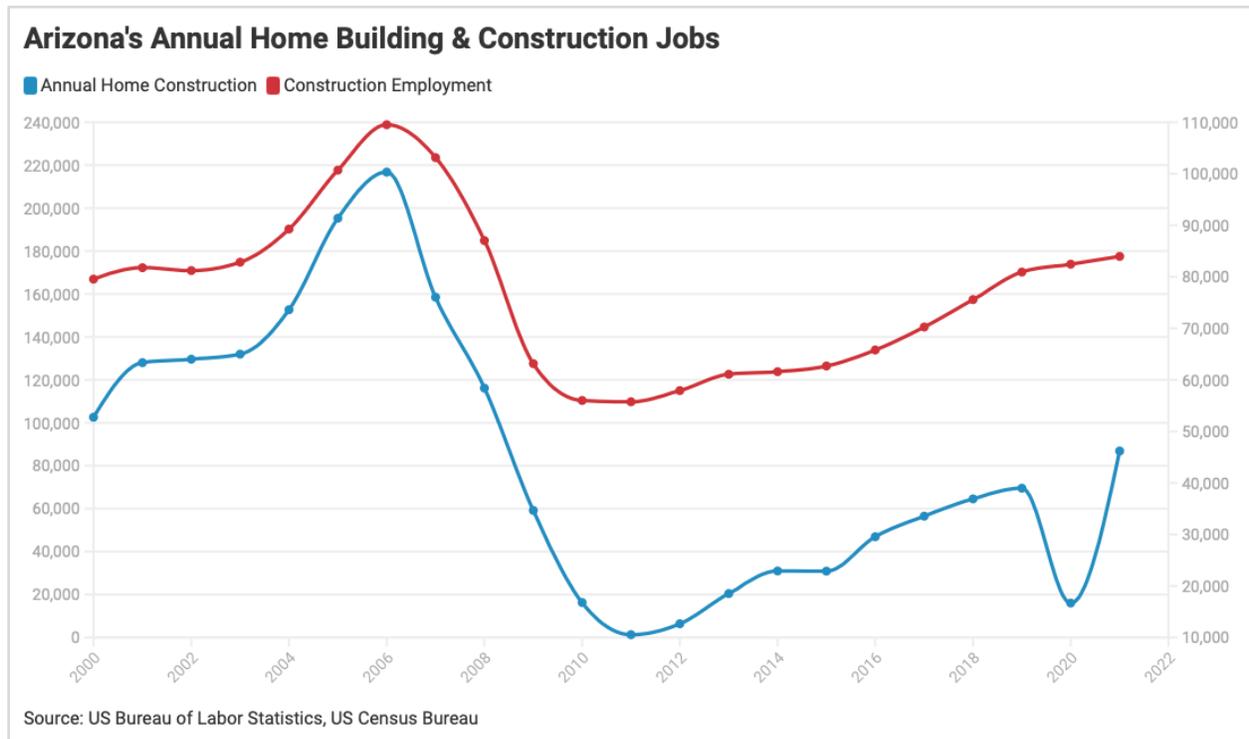
And while housing decisions are largely made at the local level, there is more the State can do to help better fund programs and policies that incentivize development and contribute to costs to build affordable housing. We also found that workforce is a major issue for Arizona developers and for cities, and the shortage of qualified workers for every stage of development and for every needed trade is only expected to get worse. While some important steps have been taken within our institutions of higher learning, more can be done to invest in these programs and in our workforce pipeline.

Taken together, we believe these steps can be championed by leaders of both parties — at the state and local level — and will better position Arizona to meet the housing and rental demand moving forward. In effect, these proposals will ensure greater economic mobility and stability for Arizona residents for decades to come and create an environment that is clear, fair, and future-focused.

A HISTORY OF HOUSING IN ARIZONA

In 2012, if someone had said that Arizona was going to experience a housing shortage in 2022 that would drive prices 50 percent higher in just eighteen months (Dec. 2020 through June 2022) and that a population and employment boom would create an environment where the state is 100,000 housing units short, they would have been laughed out of the room. And yet, just 10 years later, here we are.

Arizona was particularly hit hard by the Great Recession. In 2008, with an economy largely built around the construction industry, and with Arizona homeowners over-leveraged in debt, the foreclosure rate in Arizona according to the Phoenix Business Journal was 203 percent^{vi}. Couple that with the loss of 19,000 construction jobs in Arizona, and a drop in home

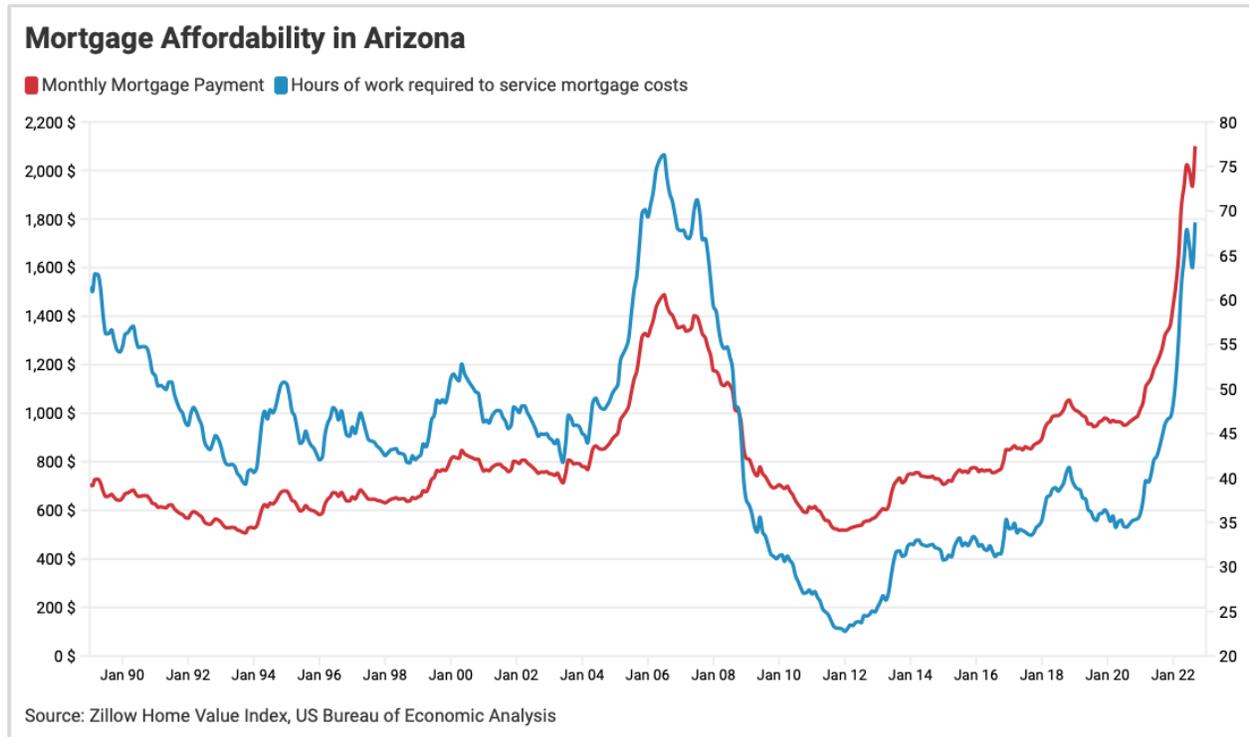


prices of 32.7% in the Phoenix Metro area between 2007 and 2008, and it's no wonder construction slowed and permits dwindled^{vii}.

Thankfully, Arizona has experienced quite the comeback. It took eight years to reach pre-recession employment levels in the Grand Canyon State, but it's been a fast rise ever since as the state has added 421,000 jobs since 2016, added \$56 billion in new Gross State Product, and seen an influx of about 600,000 new residents from outside the state. Even a worldwide pandemic couldn't stop the state, although it did experience a slowing and many industries were deeply affected. During 2020, housing construction in Arizona slowed to just 16,000 units, according to the Census Bureau^{viii} – the slowest level since 2012. But home construction sped up in 2021 and the first part of 2022 – reaching an annualized rate of 77,000 permitted units by March 2022, and putting us on track to reach the fastest pace of home construction since 2006.

Unfortunately, developer interest has since slowed with the broader real estate market. The state is likely on track to add about 53,000 units during

2022. If there is a shadow to be cast on the remarkable growth and opportunity in Arizona, it's the story of housing.

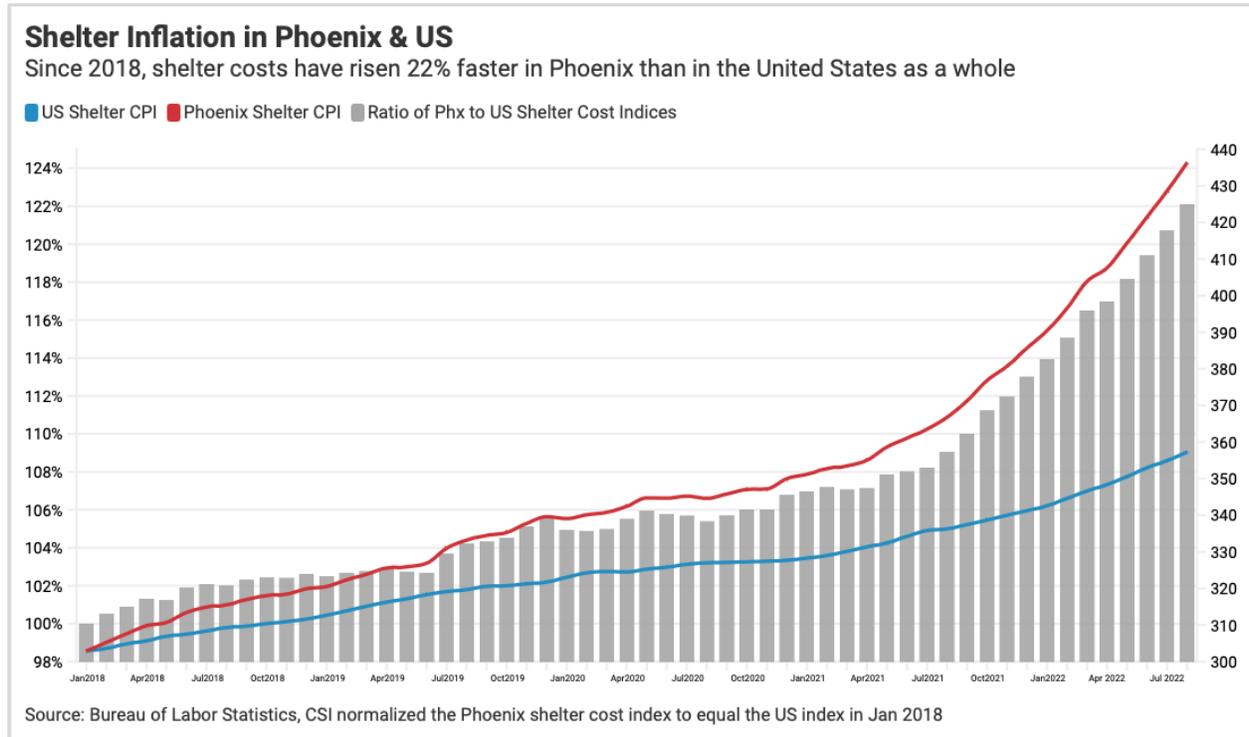


Less supply has naturally driven up prices for home sales, especially in high-demand areas in Maricopa, Pinal, and Pima counties. For Arizonans looking to buy their first home, or families hoping to move into a larger home, housing affordability has dramatically worsened in recent years, outpacing by some measures the rise in unaffordability we saw leading up to the Great Recession.

Today, the monthly mortgage payment – approximately \$2,100/month in Arizona – is higher than it's ever been. Thanks to rising hourly incomes, however, a mortgage remains relatively more affordable in terms of time (weekly hours worked) today than during the prior housing peak. Today, a typical household with a new 30-year mortgage would need to work about 68 hours/month at prevailing Arizona wages to service that debt. As a rule of thumb, we can assume that this average measure cannot sustainably exceed 72 hours given lender preference that no more than 28% of gross monthly household income go to housing costs.

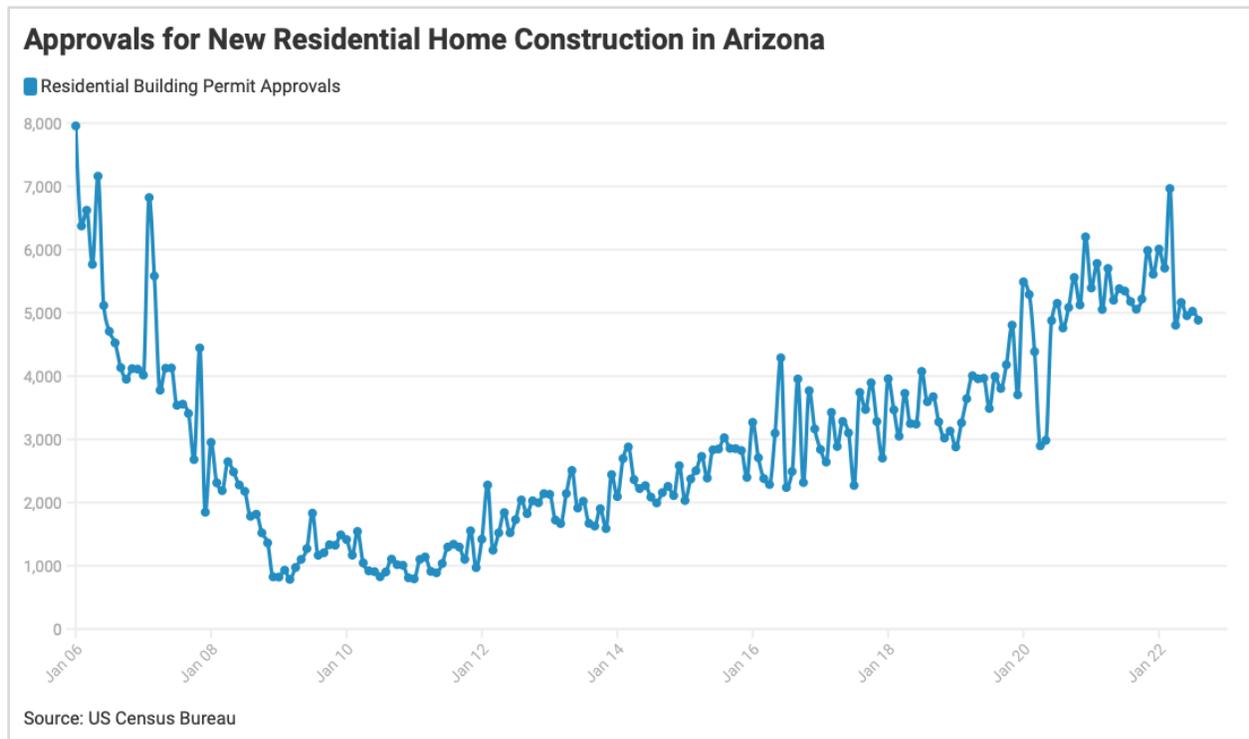
If prices and wages remain at or near current levels, however, and 30-year mortgage rates reach 7.50%, then the typical mortgage payment would require 78.5 hours of household work to make.

This imbalance has also hurt renters across the state, resulting in record increases in rental prices and the Phoenix metropolitan area experiencing



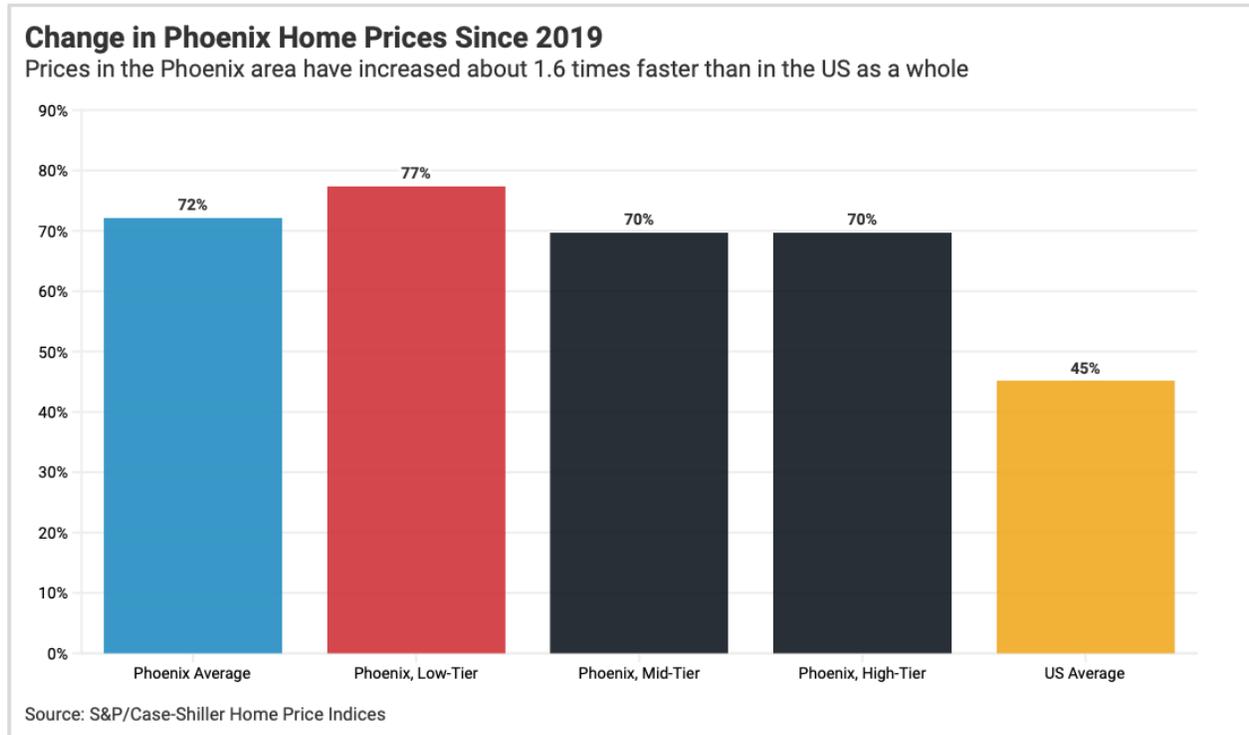
one of the highest rates of rental price increases in the country.

Today, median rent for a Phoenix area rental unit is over \$2,000/month, according to Zillow^x. This is likely because construction of new dwelling units has not kept pace with demand, depriving the market of the supply necessary to house the market's rapidly growing population. Historical data are highly consistent with a story of tight correlation between the cost of real



estate and rental rates – where rising home prices lead to rising shelter costs, though often with a significant lag^x. Therefore, it stands to reason that an improved environment for residential building construction generally will lead to naturally moderating rental prices, even if the new construction does not directly target rental or affordable units.

Still, rapidly rising rental and home prices have created stress in our communities. Change doesn't come easily. Special interests and fear of change continue to drive opposition to new housing, zoning changes, increased density, and affordable options. One mayor we interviewed said that "...it seems like every new resident to our community thinks they should be the last resident to move here." The threats for recalling local elected officials, claims of being in the "pockets of developers," and continued online bully tactics slow the already lengthy process and drive decision makers to waver.



Continued growth is critical to our state's long-term prosperity, however, we cannot overlook the increasing number of Arizona residents who are being priced out of housing of any kind.

The ability for the housing industry to rapidly respond to changing consumer preferences and local supply conditions depends on the posture of local public policy. In general, entitlement processes and residential building construction have become increasingly regulated over time, and this has made it more difficult for developers and builders to respond rapidly. Further, rising costs of construction due to, for example, code requirements mandating all units have enclosed garages, sprinkler systems, or large front and side yards are easier to pencil out in higher-tier home builds versus entry-level builds^{xi}. This leads to a particular shortage of new construction priced at or below the market median, and relegates most first-time

homebuyers to purchasing existing stock when/if it is vacated by the current occupants.

In Arizona, we like to write our own story and this situation is no different. It's time to make substantive changes in how we approach housing beginning with our neighborhoods, local governments, and the state. We like to boast of our economic development prowess and success in landing major manufacturers and having thriving industries in our backyard. Sound economic development policy must begin with sound housing policy and we have significant work to do in Arizona. Policymakers should bring the same approach – light-touch regulation, targeted incentives, and reasonable taxes, fees, and other costs of compliance – that has proved so successful in supporting its burgeoning manufacturing industry to housing development.

As of 2021, the statewide shortage of housing was 98,200 units (as estimated by CSI using local vacancy rates relative to their long-run average level) – down from 104,000 last year. A surge in the home supply deficit during the pandemic period driven by high rates of in-migration and slowing home construction has begun to close thanks to an explosion in permitting and homebuilding in 2021. As of September 2022, there were 1.7 million homes under construction in the United States – the most ever. However, permitting has fallen off, and is down over 15% from its peak. This suggests developer interest in continuing to build at the fastest rate since the Great Recession came to an end as soon as interest rates rose and buyer demand collapsed. It is unlikely at this point that homebuilding in the upcoming

years, as implied by current permitting rates, will be sufficient to close this gap and bring Arizona’s housing market back into balance.

County	2019 Deficit	2020 Deficit	2021 Housing Deficit Rank	2021 Deficit	Deficit as Percent of 2021 Existing	Annual construction needed over 5 yrs to close the gap
Apache County	(175)	(957)	5	(1,092)	3.78%	60
Cochise County	(707)	(2,193)	7	(1,424)	2.41%	385
Coconino County	1,028	(2,467)	8	(1,538)	2.20%	756
Gila County	(613)	(967)	6	(1,172)	3.60%	261
Graham County	(57)	(272)	3	(404)	2.90%	130
Greenlee County	132	(63)	1	(111)	2.52%	2
La Paz County	280	(243)	2	(379)	2.77%	(58)
Maricopa County	(40,199)	(60,514)	15	(59,186)	3.20%	42,165
Mohave County	(3,966)	(3,652)	11	(4,756)	3.98%	2,385
Navajo County	(1,485)	(922)	9	(2,229)	3.92%	554
Pima County	(8,259)	(14,796)	14	(13,324)	2.81%	6,796
Pinal County	(3,762)	(6,767)	13	(5,311)	2.96%	5,112
Santa Cruz County	(219)	(537)	4	(666)	3.51%	245
Yavapai County	(3,395)	(5,226)	12	(5,125)	4.14%	3,094
Yuma County	(2,789)	(1,817)	10	(3,347)	3.57%	1,298
Arizona Shortage	(66,939)	(104,087)		(98,192)	3.13%	63,583

Source: US Census Bureau, CSI calculations

POLICY RECOMMENDATIONS

Solving our housing crisis will require policy tools and levers at both the local and state levels. Arizona’s current practice grants local municipalities considerable autonomy over zoning, entitlement, and permitting processes – resulting in a confusing hodgepodge of systems, definitions, fees, and timelines depending on the jurisdiction where a project occurs. On the other hand, strict state pre-emptions have deprived local governments of any authority to experiment or utilize at all certain potentially powerful policy levers.

Local government truly has an ability to influence the housing crisis in substantial ways. Through process changes, efficiencies, creativity, and political will, local governments have the opportunity to streamline approval and get more units built quickly. Their efforts will be crucial to addressing

our supply crisis and building more housing at both affordable and market rates.

At the same time, the state should revisit certain statutory prohibitions that prevent local governments from encouraging the development of new housing, or preserving the supply of existing housing, within their jurisdictions. The state can also be helpful by using its resources to assist with financing of affordable housing projects and funding greater supply themselves. These levers include permanent funding of the state Housing Trust Fund (HTF), a statewide grant program to incentivize cities to create dedicated funds for affordable housing, and additional investment in workforce training through our community colleges to help train the workers needed for housing construction and related expertise.

Expedite Zoning and Entitlement Processes

One of the most discussed barriers to bringing housing and development to market is the lengthy and technical municipal entitlement process - the process of obtaining municipal approval to develop a piece of property which may include minor and major general plan amendments, annexations, and rezoning. Current processes vary from city to city with conflicting opinions on which process is the "best practice." All can agree, however, that the process is burdensome, costly, and takes far longer than is practical from a development perspective.

By developing a streamlined process, universal to all Arizona cities, the consistency achieved would allow for a more objective, less nuanced approach. The development of a uniform process at the state level should be collaborative in nature among cities and consider cities of all sizes. Builders and developers would go through the same process regardless of the jurisdiction, and get more houses to market faster.

The new streamlined processes would consist of both general guidelines local governments are recommended to follow and specific statutory requirements local governments would be required to comply with.

Streamline Design Review Processes

Like the entitlement process, the design review process can add costly time to development. Ensuring that the process is fair, objective, and timely while still honoring the character and personality of individual municipalities will serve as an accelerator to bring housing and other development to market more quickly. While some cities and counties don't currently require a design

review, they would retain the ability to require or abstain from such processes according to local needs.

However, any city that did require design reviews would need to follow statewide standard guidelines to ensure the process was efficient, objective, and consistent.

Empower the State Department of Housing to Grade Local Processes

Once the state has designed and implemented statutory guidelines around streamline entitlement, review, and permitting processes for residential development, the Department of Housing would be required to review and monitor local processes and grade municipalities using an objective standard.

The standard would consider how long, expensive, and onerous an entitlement, design review, and permitting process for residential development was. In reviewing the onerousness of this process, the Department would compare the cities performance relative both to other cities and towns in Arizona, and national benchmarks and standards. For example, the Department would consider:

- What a city or town's fees for permits, entitlements, and other required licenses or permissions are, relative to those charged by other cities.
- Processing time between application and final response – approval or denial – by a city or town to a permit, entitlement, or other application.
- Application complexity, in terms of number of hours required to complete needed applications.
- Number of licenses, fees, or approvals required between initial planning and actual construction of new housing development.

Only high-performing cities and towns would be permitted to avail themselves of certain new privileges permitted them under the state's holistic affordable housing development package. Local grades would be updated annually according to a process specified by the Department.

Develop Universal Statewide Zoning Definitions

Zoning definitions vary from city to city. Multi-family definitions may include ten units per acre in some cities or fifty units in another. Single family home zoning definitions vary from city to city. Identifying logical and predictable zoning definitions at the state level allows for comparison of zoning between municipalities, transparency in the process, and clarity for developers. In

addition, defining new or innovative types of housing, diversifying the types of housing within a municipality, and providing a cohesive way to update municipal codes will benefit cities, regions, and developers. For example, having statewide guidance on accessory dwelling units (ADU's) would give greater clarity to local governments about adding units to existing properties that could help increase supply.

Identify Reasonable Schedules for County and Municipal Reviews with Penalties for Failure to Perform

Developing timely schedules for reviews and approvals as it relates to entitlement, design review, and building permits is a key component of the local contribution to bringing housing to a community efficiently. Most communities post their turnaround times for standard processes. Some communities have expedited processing for a greater cost. In the event of a delay, there is currently no penalty for a city or town that doesn't meet its own defined schedule.

For example, if a re-zoning application is submitted, a city may have a posted turnaround time of 30 days. If the comments are returned to the developer in 45 days instead of the posted 30, there is no consequence. Further complicating matters are the posting requirements for public hearings, agenda deadlines for public bodies, and the management of a variety of professionals whose expertise and skills are necessary to bring a plan to submittal. Coordinating such activity with unpredictable timing from municipalities can set a project behind in schedule by months.

Local governments must be held accountable for delays. A monetary penalty, refund of a portion or entirety of the city fee to the developer, or other mechanism for accountability can and should be employed.

A key component of this recommendation includes both parties signing off and committing to schedules, the "clock" only starting when all items are submitted by the developer and accepted as "complete" by the city and ensuring that there are enough city staff to meet the demand as the market ebbs and flows.

Limit the Number of Plan and Design Reviews and Re-inspections Focused Solely on Life and Safety Issues

It is not uncommon for there to be multiple plan reviews throughout a process. However, on occasion, the number of reviews can become excessive and significantly delay a development with minimal or zero benefit to the community. While there may be "red lines" on a site plan after first

review, highlighting the need for changes, the developer's architect or engineer is sometimes left having to decipher the intent of the reviewer.

For example, if the local Fire Marshall reviews a site plan and determines that the width of the fire lane is not to code, they may note on the plan that the fire lane must meet code triggering a re-submittal. However, upon adjusting the width of the fire lane, there must be two feet removed from the perimeter landscape buffer to accommodate the additional width. Upon second submittal, it is noted that the landscape requirement now doesn't meet code. Where should there be a practical accommodation? The alternative site plan adjustment may be to shift buildings resulting in less amenity or open space for the residents. If all cities prioritize the life and safety issues above all else, flexibility and common-sense solutions can be granted.

Furthermore, limiting the total number of times that cities and developers can exchange plans will cut down on unnecessary delays, reduce petty adjustments from both sides, and force needed dialogue to develop mutually beneficial solutions.

Universally Allow for Self-Certification and At-Risk Construction Activities

Building housing requires professional engineering seals of approval on all plans. Such professionals are accountable for their work. There are occasions and situations in which allowing professionals to self-certify their work should be encouraged rather than waiting for city engineer approval.

The question of liability is always identified as a hinderance to self-certification. However, there can be waivers and/or city certification programs that qualify an individual to self-certify.

To move forward with development on a timely schedule, it may be necessary for a developer to proceed with various aspects of construction on an "at-risk" basis, meaning they are proceeding with on-site work and are assuming all costs without yet receiving necessary city approvals. This is considered a best practice and, when done within parameters, can save valuable time in the process bringing housing and other development forward more quickly.

Remove Municipal Adoption of Building Codes and Allow the State Registrar of Contractors to Adopt Codes for the State

Approval of International Building Codes can be a complex process. Inevitably, some updated and recommended technique or material is seen as an improvement while others are considered antiquated and irrelevant. Mayors and Council-members are, most often, ill-equipped to be weighing in on the validity of a construction method. Furthermore, some of the sections of the International Building Codes don't apply to the Arizona region or would be counter to our state's goals.

Developing and adopting a set of Arizona or regionally significant building codes will take industry professionals and experts. Removing politics and seeing the codes through the lens of someone in the industry creates a seamless set of building codes adhered to in every jurisdiction.

Within the Entitlement and Design Review Process, Require Cities to Hold a 30-day Public Comment Period

In today's environment, citizen activists and concerned neighbors are engaging regularly in city entitlement and design review processes. In many cases, citizen input improves development plans, creates opportunities for community buy-in, and helps developers understand local market dynamics. In other cases, citizens who aren't regularly engaged in the process can be overwhelmed, driven by emotion, and base their response on personal interpretation instead of facts. Due to the many city and developer touchpoints required through plan approval, the resident may feel their voice is lost or ignored.

Contributing residents and stakeholders deserve to have their voice be heard, to share their perspective, and to be an influence on the decision-making process. Developers and property owners deserve the opportunity to disseminate factual information, to respond to questions and concerns, and to navigate the city process without undue delays.

By providing a set, 30-day citizen review period embedded into the process, citizens and stakeholders would have an opportunity to submit questions and share opinions about the merits of a case. By creating structure and order, citizens can verify that their comments were received, view real-time responses, be included in the public record, and provide for efficiency in public meetings. Furthermore, no citizen will be left out of the process due to ability, time constraints, lack of transportation, financial reasons, or for any other purpose. With a 30-day citizen review and various modes of

contribution to the public record, residents and developers can seek common ground and ideally move forward with development.

Create Reasonable Schedules and Response Requirements for State Agencies and Other Requirements with Penalties for Failure to Perform

On occasion, there may be a need to interact with other governmental bodies for permits or to sign-off on various regulatory requirements. As cities are held accountable, so should state agencies. By developing feasible response schedules and deadlines that can be incorporated into the overall process, all parties are invested.

Penalties for not adhering to the schedule and deadline can and should be implemented.

CHANGES TO STATE LAW TO INCENTIVIZE LOCAL DEVELOPMENT

Amend the State Statute on Inclusionary Zoning and Permit Cities and Counties to Allow Affordable Units if a Developer is Reimbursed for the Cost of the Subsidy

This would require amending Arizona Revised Statutes (ARS) Title 9 Section 461.16 relating to cities and towns, and ARS Title 11 Section 819 for counties. This change would allow a city or county to partner with a developer to include a percentage of units in a development to be affordable (rents or sales prices charged on some of the units being below-market) if the developer were compensated in-kind for any costs associated with the below-market subsidy. Compensation could take the form of city tax relief, waiver of permit or other local development fees, or waiver or expedition of permits or other local processing requirements. Both the developer and the local government would have to agree to the plan and attest that the local compensation fully offsets the costs associated with the inclusion of affordable units.

The local government must further have received a high-performing grade from the state's Housing Department, certifying that it has a streamlined, efficient, and reasonable permit and approval process for residential development.

Several states, including Florida, have passed similar legislation in recent years. This approach reflects a compromise between two competing philosophies around inclusionary zoning: the state should either ban it

entirely or local governments should require developers to include affordable units and not compensate the developer for the loss in revenue.

Allowing local governments to implement inclusionary zoning, however limited in scope, will increase the number of affordable units on the market at a time when housing and rental costs are increasing for many Arizona families. Furthermore, the affordable housing units will be integrated into the community removing the stigma and negative social impact that can accompany affordable development.

Allow Local Governments to Form 'Housing Opportunity Zones'

While cities need to improve their processes, we acknowledge they need additional tools to add houses. One way to provide this is through 'housing opportunity zones'. These districts would be created within a municipal boundary for the express purpose of improving the supply of housing in areas and circumstances where the market alone is unable to meet demand.

If approved by the state Department of Housing on request of a city or town, a 'housing opportunity zone' uses a percentage of existing tax revenue from within the district to help fund development, like residential housing construction, infrastructure upgrades, or other needed capital expenditures. This tool would likely be most popular in areas that are ripe for development where there are already significant resources being invested in bringing more housing supply on to the market. Adding this capability gives cities another tool to add additional housing supply and reduce prices in their municipalities. Like all policies of this nature, it should have a sunset date and be reviewed by the legislature.

Only developers who construct housing and meet accountability benchmarks could retain a proportion of local sales or property taxes otherwise owed on the project to compensate it for costs associated with building and selling the affordable units. A city or town could also use the monies to reimburse itself for capital costs associated with providing public infrastructure that supports these projects.

In order to be eligible to create such a district, the local government must demonstrate that insufficient housing is being provided within its proposed boundaries to meet market demand at an affordable price, and that the creation of the district would credibly increase housing supply and reduce housing prices relative to the baseline. The local government must further have received a high-performing grade from the state's Housing Department, certifying that it has a streamlined, efficient, and reasonable permit and approval process for residential development.

Reform State Laws Relating to Short-Term Rental Properties

Passed with near unanimous support in 2016, the state's law prohibiting local governments from regulating short term rental properties has had a host of unintended consequences for policymakers, neighborhoods, and housing prices.

The convenience of short-term rental properties has led to new business opportunities for investors and Arizona families with properties available for rent. What once began as a niche market has exploded in popularity in recent years, with short term rental properties rapidly growing as a share of all residential property in many neighborhoods throughout the state, particularly in high-demand areas like Sedona, Flagstaff, Paradise Valley, and Tempe.

This increase in demand for short term rental properties has impacted the supply of housing. Residents who take their concerns to their local elected officials are told that the state legislature took their authority to regulate these properties away from them. Fewer homes that are available in these areas for longer-term rent or purchase is impacting supply in already underserved areas, helping drive up prices for residents in those very same neighborhoods. Any discussion around the lack of housing supply needs to include short term rental properties and the relative data.

Recent changes to state law, including a bipartisan bill passed earlier this year restoring some autonomy to local governments, are welcomed. However, regulations around neighborhoods and zoning are normally reserved for local governments, not the state. Every municipality is different and carries with it different needs and local concerns. Our recommendation is that the regulatory parameters for short-term rental properties should reside at the local level, and not the state legislature.

A state framework that prohibits local governments from banning private property owners from renting out their homes entirely is reasonable and – based on experience – necessary. Short of that, local governments need additional tools and sufficient authority to further regulate the space to ensure a supply of local short-term rentals does not interfere with the quiet enjoyment of traditional long-term residential units. Local governments need these tools to better respond to their constituents and ensure that additional rental and sale units are available, helping to drive down housing costs in their municipalities. This will help protect the housing market from undue burdens imposed upon it by short-term rentals.

Give Public School Districts More Flexibility on Land Proceeds When Selling Property

When public school districts sell excess land, they can only use the proceeds from those sales for capital projects like school construction or renovations (ARS Title 15-1102). This limits the ability for school districts to utilize the dollars for what is most needed like providing pay raises for teachers, hiring needed support staff, or upgrading curriculum.

By giving school districts greater autonomy on the proceeds that could occur when selling excess land, this would potentially free up additional land for housing development, particularly in urban areas.

This policy change would be a win-win: school districts could use the proceeds to help recruit teachers and address short-term funding needs, and more land would be available for additional housing supply.

Any land sale would still need to be approved by the voters within that school district during the next bond election, ensuring residents have oversight on the transaction. The process of re-zoning sold school district lands to allow for other uses – like housing development – should be expedited and made easier ahead of the sale. These restrictions lower the market value of the land and make it more difficult for developers to use the acquired property for housing development.

STATE FUNDING INCENTIVES TO ENCOURAGE DEVELOPMENT

Permanent On-Going Funding for the State Housing Trust Fund (HTF)

Administered by the Arizona Department of Housing, the HTF is a fund dedicated to investing in affordable housing projects. It is the most reliable and effective policymaking tool we have to help build more affordable housing statewide.

Before the Great Recession, the state legislature appropriated dollars to the HTF on an annual basis. Recent investments have only been one-time allocations, with \$15 million appropriated in 2019 and \$60 million earlier this year.

By adding a permanent on-going appropriation going forward, the HTF can regularly help fund and finance affordable housing projects throughout Arizona and provide developers and builders a greater sense of certainty

that investment and support from the state will be guaranteed in future years.

Fund A Statewide Grant Program to Incentivize Cities to Create Dedicated Funds for Affordable Housing

In addition to dedicated statewide funding for affordable housing, the state should be encouraging cities to create their own affordable housing funding at the local level. One way to do this is to create a statewide grant program that incentivizes cities to create dedicated funds that would go towards more affordable housing development.

The city of Tempe has been a leader in this regard, creating their Hometown for All program in 2021. Fifty percent of several development permitting fees paid to the city go into the fund and help finance land acquisition and redevelopment within city borders.

The amount of the grants would be up to the legislature and could cover seed funding for the programs or reimburse local governments a specific dollar amount. The important concept is that the legislature supports these initiatives at the local level and uses its resources to assist them to create more affordable housing supply where it is needed.

Fund a Statewide Grant Program to Incentivize Cities to Streamline Rules and Regulations Around Housing Development

In line with the reforms to local zoning and approval processes outlined above, the legislature should consider creating a dedicated fund that local governments could apply for if they meet specific criteria around approving more housing units and streamlining regulations.

With demand at record highs, there should be every incentive in place for local governments to approve more construction and add supply to our housing market. Municipalities that go above and beyond to think of new innovative approaches to solving this crisis should be rewarded and serve as a model that other local governments can follow. Creating a fund to reward cities for improving their housing stock is one way to do that.

Increase State Funding for Housing and Construction-Related Workforce Programs

Even with greater housing supply and financing options, the state would still need a larger trained workforce to help build the homes and units needed to address our housing crisis. The state can do more to help ensure that this

workforce is trained and ready for this, and that includes investing additional dollars in our workforce development programs at our community colleges.

The state has been reluctant to increase on-going funding for higher education in recent years, often defaulting to one-time investments for both our universities and community colleges. Recent investments in the Arizona Board of Regents' New Economy Initiative (NEI) and on-going funding for STEM programs at our Maricopa and Pima community colleges have been encouraging and serve as a model for what the state could do to tackle its construction workforce shortage.

Our state community colleges serve as an invaluable partner in our workforce development pipeline, and the housing industry is no exception. These colleges already provide programs in specialties like construction trades, construction building codes, construction design, building inspection, and welding. Targeted investments from the state to expand and grow these programs will help train the additional workers necessary to meet demand in future years.

Water Infrastructure & Security

From our stakeholder conversations, it was readily apparent that access to affordable, plentiful, and sustainable sources of water was a critical component of the state's long-term housing supply. But we also recognize that this is a critical issue for state economic development generally.

We believe this issue is best addressed in a targeted and holistic fashion that focuses on all the issues in Arizona's water market, rather than in a patchwork response that looks at – for example – just the needs of the housing market. Common Sense Institute should explore state water policy more thoroughly in a future paper.

We hope any exploration contemplates existing inequities in water policy with respect to housing development that, for example, create an unfair playing field for multi-family versus single-family development.

CONCLUSION

Arizona is blessed to feature a competitive business environment, quality way of life, and a growing economy. The state has spent considerable resources to create an environment where businesses and families want to call our beautiful state home. Its best years are ahead of it.

However, without enough housing supply for both home buyers and renters, Arizona will struggle to reach its full potential. Both the state and local governments have failed to create a policy environment where housing can be approved quickly, efficiently, and transparently.

These failures have led to record increases in both housing prices and rent. When coupled with high inflation because of the COVID-19 pandemic, families are struggling to afford to buy a home or pay rent. While these problems are present across the country, Arizona's high influx of transplants from other states, and our growing economy, have made the pain particularly acute here at home.

To help solve this crisis, significant reforms will need to be considered and implemented at both the local and state levels. It will require an all-of-the-above approach that brings local governments and the state legislature together to create a cohesive plan to build more housing where it is needed to help bring down rental prices and stabilize prices for home buyers.

Our recommendations are designed to provide both local governments and the state legislature with the tools and policy changes they need to seriously tackle this crisis. Pleas to build more housing in years past have seen leaders reply that they do not have the tools to adequately address this problem, or that their hands are tied by another branch of government. Success is contingent upon collaboration with the private sector and a concerted effort by investors and developers to utilize the tools and processes available in a responsible way.

If our recommendations are adopted, the time for those excuses will be over. Reforming local entitlement processes, being accountable for timelines and schedules, and adopting universal definitions for development will give developers the clarity and simplicity they need to build housing at a rate that meets market demand. Removing state preemptions around inclusionary zoning, creating 'housing opportunity zones', and further regulating short-term rentals will provide local governments with the tools they say they need to approve more projects. And investing additional dollars at the state level will maximize the policy levers the legislature can adopt to assist with funding and developing projects locally.

We love our state, and we want to see it succeed. For Arizona to reach its full potential, solving our housing crisis is of critical importance. Taken together, these policy recommendations would steer our state in the right direction and give policymakers and leaders at all levels the tools, resources, and clarity they need to enable for additional supply and stabilize our housing market at a time when Arizonans need it most.

APPENDIX: Acknowledgments & Stakeholders

CSI and our Fellows would like to thank the following list of housing sector experts and stakeholders for their time and contributions to the preparation of this report.

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