# New Study Shows Impact of Government Fees On Home Affordability

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The National Association of Home Builders sponsors an economic publication for the housing industry which publishes at HousingEconomics.com. In mid-July it **released a study** on *Metropolitan Area House Prices and Affordability* written by Elliot F. Eisenberg, Ph.D.

One cannot deny that the study is self-serving, but the findings are at least a little revealing of some of the reasons that housing prices, particularly of new houses, continue to climb in a tough market.

The study looked at what happens to **housing affordability** in 357 Metropolitan Statistical Areas (MSAs) whe house prices rise. Because over 80 percent of home buyers purchase using a mortgage, the ability to qualify fo loan is a major determinate of affordability. Therefore, the study changed the price of a representative home i area and estimated how many people/households that qualified for a mortgage before a hypothetical $1,000 p increase would fail to qualify afterward.

While results varied geographically, overall the study found that using typical assumptions - a 10 percent down payment, private mortgage insurance, 30-year fixed-rate mortgage, local information about property taxes fro census data, insurance pricing from the National Association of Insurance Commissioners and the Insurance Information Institute, and underwriting standards as approved by Freddie Mac and Fannie Mae - a $1,000 incr in the median price of a house would price 217,000 households nationally out of the market. These numbers v by MSA from a low of 10 households in both LaCrosse, Wisconsin and Ocean City, New Jersey, to 4,193 house in Dallas-Fort. Worth.

An increase in prices has a greater impact where large numbers of people have the ability to purchase a house given price. The more expensive the area the fewer households are affected by a price increase. Therefore, th is much less impact in communities where houses are already relatively high priced.

For **example**, in the San Jose-Sunnyvale-Santa Clara, California MSA only 0.8 percent of the total of 597,597 households can afford a median-priced home which costs $849,022. The $1,000 price hike cuts out 313 households. In the Salinas, California MSA 3.5 percent of 123,630 households can qualify to purchase a media priced new home at $669,091; a price increase eliminates only 31 of them.

At the other end of the spectrum is Charleston, West Virginia where 66.9 percent of the 125,779 households a estimated to be eligible for a mortgage on a median priced house which is estimated to cost $85,804; raising t price by $1,000 cuts 463 households out of the equation. In Morristown, Tennessee 61.2 percent of 54,486 households can currently afford to purchase a median priced new house at $97,640 and 239 of them would los that ability with a $1,000 increase in the purchase price.

The gist of this affordability study, however, is the impact of **government fees** on affordability. "For example, time a local government raises construction costs by increasing the price of a construction permit, a tap fee, a proffer or an impact fee, the cost of building a house in that area rises and affordability is necessarily reduced.'

And the increase in home price will usually be more than the increase in the government fee itself. Citing that construction financing costs and real estate agent fees rise in tandem with any increase in actual construction costs, the study speculates that prices will rise about 22 percent more than the underlying expenses.

The study's author points out that most government fees are paid early in the construction process, many befo any work has begun at all and offers the following hypothetical example of how a $1,000 increase in house pric would come about.

Assuming an increase in construction fees of $819 (the number is arrived at by backing out of the $1,000 price increase), an average annual interest rate for construction financing of 10 percent, and a total time from

authorization of construction to sale of the property of 11.8 months (7 months from authorization to completio
4.8 from completion to sale) would add $80.54 to the $819. The price increase would add an increase in the average brokerage fee of $23.75 and the builder's compensation and profit of 9.30 percent would add $76.17 f sum of added costs of $180.45 or a total of $999.45.

When the costs of a median-priced new house rises, the study says, prices of existing houses rise as well. Thus affordability across all price levels is reduced when building fees are raised.

We all see where this is going, of course; a drive on the part of **NAHB** to roll back or at least cap permit fees, school fees, road fees, and other infrastructure related fees that are paid by builders. Still, the construct is an interesting one. The results, in the words of the author do not answer questions "such as 'How many househol will not buy a house when they otherwise would have?' or 'What will the resulting reduction in home constructi be?' To answer those questions requires an economic model that also incorporates the willingness of househol buy smaller houses, older houses, and houses that have few amenities."

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Story Information

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