

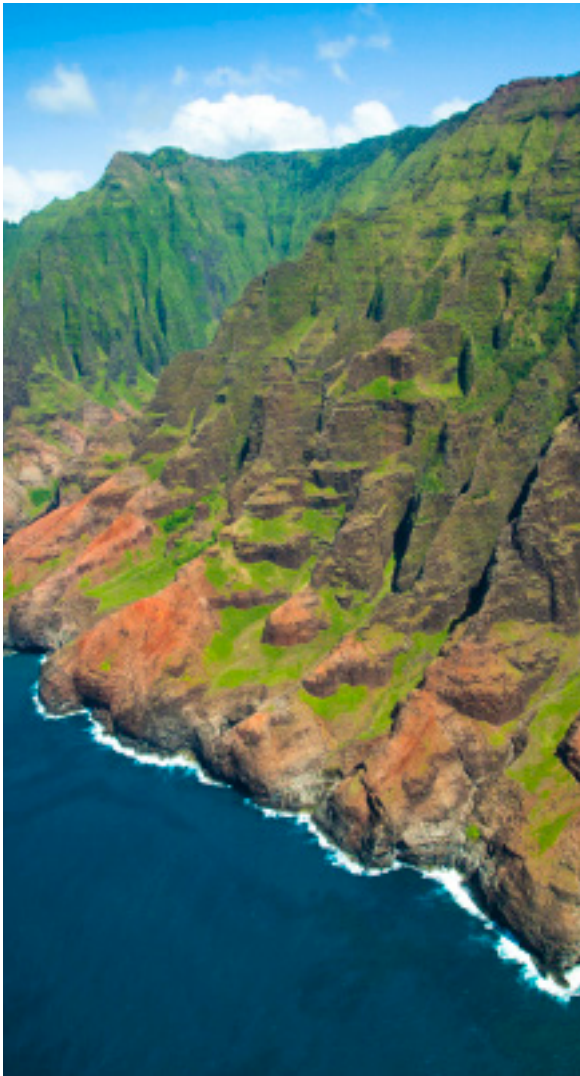


THE ECONOMIC RESEARCH ORGANIZATION  
AT THE UNIVERSITY OF HAWAII

UHERO REPORT

## THE MAUI COUNTY COMPREHENSIVE AFFORDABLE HOUSING PLAN: UNDERSTANDING ITS PROS AND CONS AND IDEAS FOR HOW TO IMPROVE IT

OCTOBER 21, 2021





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**The Maui County Comprehensive Affordable Housing Plan:  
Understanding its Pros and Cons and Ideas for How to Improve it**

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## EXECUTIVE SUMMARY

A team of 19 planners, engineers, data and policy analysts, attorneys, and community development professionals has developed a comprehensive plan for the development of affordable housing in Maui County. The Maui County Comprehensive Affordable Housing Plan (“MCCAH Plan” or “the Plan”) is a major step forward in developing coherent strategies to address Maui County’s shortage of affordable housing for lower-income households.

- The MCAAH Plan uses estimates from the 2019 Hawai‘i Housing Planning Study (SMS Research, 2019) to determine how much and what mix of housing is needed in Maui County.
- The Plan presents an ambitious road map for reforming Maui’s regulatory framework governing the development of affordable housing and proposes a goal of building 5,000 affordable units within five years of the Plan’s launch.
- The Plan identifies specific county-owned and state-owned land parcels on which 4,333 of the 5,000 affordable units would be built.
- The Plan identifies zoning and permit regulations and procedures that need to be streamlined and updated to facilitate timely completion of affordable housing projects.
- The Plan clearly identifies complementary infrastructure investments that should be made simultaneously to support the new affordable housing projects.

The cost of the overall Plan is estimated to be \$1.169 billion. To support these expenditures, the Plan proposes substantial increases in real property taxes on non-owner-occupied residential properties and short-term vacation rental properties as well as a new form of assessment on developers of all other residential properties. It is estimated that \$58 million in new annual tax revenue over a thirty-year period would be needed to service bonds sold by the county to finance housing and infrastructure construction and to support ongoing expenditures directed to mortgage subsidies and rental subsidies to support low-income households in buying or renting housing.

- We strongly suggest that a few key components of the Plan be modified to ensure its proposed “by-right” regulatory framework for approving, planning, and developing land parcels with affordable housing does what the Plan’s authors intend: Increase the flow of new affordable housing units coming to market over the next 5-10 years.

We recommend two other substantial changes to the Plan to ensure that its execution does not impede the private development of housing. The changes are important because the housing needs of Maui’s lower-income households can only be partially met by the additional affordable units to be developed by the County. Families across the Maui income spectrum need additional units to be brought to market by private landowners and developers.

- To accomplish this, we recommend that the “by-right” regulatory framework proposed in the Plan be extended to property owners remodeling existing multi-family units and to private development of new multi-family projects.
- We recommend that the County take a close look at project financing by reviewing the sources of tax revenues required for the project, restrictions on the use of bond revenues, and reconsider exactions from developers building market-rate units.



With these modifications, we conclude that the Plan provides a useful roadmap to developing affordable housing and easing the impact on lower-income households. The time frame for the Plan is ambitious but may be possible if the (suitably modified) up-front regulatory changes are enacted within the next 18 months.

## **THE MAUI COUNTY COMPREHENSIVE AFFORDABLE HOUSING PLAN: UNDERSTANDING ITS PROS AND CONS AND IDEAS FOR HOW TO IMPROVE IT**

A team of 19 planners, engineers, data and policy analysts, attorneys, and community development professionals has developed a comprehensive plan for the development of affordable housing in Maui County. The Maui County Comprehensive Affordable Housing Plan (referred to as “MCCAH Plan” or “the Plan” throughout this document) is a major step forward in developing coherent strategies to address Maui County’s shortage of affordable housing for lower-income groups. The MCAAH Plan uses estimates from the 2019 Hawai’i Housing Planning Study (SMS Research, 2019) to determine how many and what mix of housing units are needed in Maui County. Based on these estimates, the Plan presents an ambitious agenda for reforming Maui’s regulatory framework governing the development of affordable housing and proposes a goal of building 5,000 affordable units within five years of the Plan’s launch. The Plan identifies specific county-owned and state-owned land parcels on which 4,333 of the 5,000 affordable units would be built. The Plan identifies zoning and permit regulations and procedures that need to be streamlined and updated to facilitate timely completion of affordable housing projects. It clearly identifies complementary infrastructure investments that should be made simultaneously to support the new affordable housing projects. The cost of the overall Plan is estimated to be \$1.169 billion. To support these expenditures, the authors of the Plan propose that the County of Maui government impose substantial increases in real property taxes on non-owner-occupied residential properties and short-term vacation rental properties as well as a new form of assessment on developers of all other residential properties. It is estimated that \$58 million in new annual tax revenue over a thirty-year period would be needed to service bonds sold by the county to finance housing and infrastructure construction and to support ongoing expenditures directed to mortgage subsidies and rental subsidies to support low-income households in buying or renting housing.

The MCCAH Plan is notable for its attention to detail in identifying particular parcels for affordable housing development and its proposals for reform of the regulatory process for planning and vetting affordable housing projects. It explicitly borrows institutions and regulatory mechanisms used by other high-cost comparable-size communities in the western United States to bring more affordable units to market. The Plan centralizes the planning and development of affordable housing within a new position in the Mayor’s cabinet, the Affordable Housing (AH) Coordinator, and provides the AH Coordinator with resources to plan and develop new units. To promote efficient use of county resources, a Community Oversight Board (COB) is tasked with both decision-making regarding project selection and monitoring activities of the AH Coordinator. Whether the COB has sufficient incentives and capacity to adequately monitor the affordable housing projects it commissions is critical if county resources are to be used efficiently. It is important that the Council also monitor resource use by the AH Coordinator as government oversight boards are often limited in their willingness to monitor closely-affiliated officials. It is also important that the County does not rely solely on the public sector to develop affordable housing and that the Plan includes mechanisms for strengthening affordable housing development by the private sector.

We strongly suggest that a few key components of the Plan be modified to ensure its proposed “by-right” regulatory framework for approving, planning, and developing land parcels with affordable housing does

what the Plan's authors intend: Increase the flow of new affordable housing units coming to market over the next 5-10 years. We recommend two other substantial changes to the Plan to ensure that its execution does not impede the private development of housing. This is important because the housing needs of Maui's lower-income households can only be partially met by the additional affordable units to be developed by the County. Families across the Maui income spectrum need additional units to be brought to market by private landowners and developers. To accomplish this, we recommend that the "by-right" regulatory framework proposed in the Plan be extended to property owners remodeling existing multi-family units and to private development of new multi-family projects. Finally, we recommend that the County take a close at project financing by reviewing the sources of tax revenues required for the project, restrictions on the use of bond revenues, and reconsider exactions from developers building market rate units. With these modifications, we conclude that the Plan provides a useful roadmap to developing affordable housing and easing the housing crunch felt by lower-income households. The time frame for the Plan is ambitious but may be possible if the (suitably modified) up-front regulatory changes are enacted within the next 18 months.

This report reviews and evaluates key provisions essential to the Plan's future operation. The bullet-pointed bold text comes directly from or summarizes a key provision of the plan; the non-bolded text that follows is our commentary on that provision.

- **Plan uses estimates of affordable housing need from 2019 Housing Planning Study by SMS Research**

The plan takes estimates of need for affordable housing from SMS's 2019 Housing Planning Study and accepts them as measures of actual demand for affordable housing. As a result, the Plan sets very specific targets— 15% of homes to be delivered for households with income between 80 and 120% Area Median Income (AMI), 35% for households earning 50% to 80% AMI and 50% of homes for households below 50% AMI. We caution that these estimates are subject to significant uncertainty and should not be interpreted as representing firm demand for homes. To the extent that economic conditions and personal finances of households on Maui do not result in the demand envisioned in the Plan, developers and the county may face losses that will inhibit housing development and the overall success of the Plan. It is important to recognize the uncertain nature of these "housing demand" estimates and build more flexibility into the Plan.

- **Appoint a cabinet-level affordable housing coordinator to serve in the mayor's office to oversee implementation of the plan.**

The Plan recommends that the County create a new position, the Affordable Housing (AH) Coordinator, who would serve in the Mayor's cabinet and be directly responsible to the Mayor. The AH Coordinator is charged with overseeing the legislative implementation of the new affordable housing regulatory framework, working with and serving on the Community Oversight Board (see below) to vet and plan affordable housing projects detailed in the Plan, managing affordable housing construction by private-sector developers, and coordinating and monitoring off-site infrastructure projects undertaken by other Maui agencies. This recommendation is well founded given the large portion of county revenues that the Plan dedicates to the new affordable housing construction and household assistance programs. It is important that the position be outside of particular county departments because building affordable housing necessarily involves coordinating activities of and resolving disputes between several departments. Concentrating responsibilities

for affordable housing activities around a single position (and support staff) should make it easier for the County Council and public to monitor program progress.<sup>1</sup>

- **Create a community oversight board (COB) to target and monitor investments from the Affordable Housing Fund and manage the affordable housing coordinator.**

The Plan assigns to a COB the responsibilities of identifying and ranking affordable housing projects and managing the process of developer selection. Placing these responsibilities within a COB is important for several reasons. First, the COB should increase transparency for the decision-making process given the COB's public meetings and ranking process. The Plan correctly emphasizes that the public and transparent nature of the COB decision-making process should force more accurate rankings of potential land parcels than the more opaque decision-making of the Maui County Dept. of Housing and Human Concerns (pp. 25-26, 46). Second, the COB brings stakeholders from different parts of the community into the decision-making process, and this diverse representation should help bring more information to bear in land-selection and developer-selection decisions. Third, the COB also brings another source of monitoring for the activities of the Affordable Housing Coordinator.

For the COB to function properly, it needs to avoid the two extremes of being a rubber stamp for the AH Coordinator or attempting to micromanage planning and development of the county's affordable housing projects. Rather it should be tasked with selecting lands for affordable housing projects and monitoring the activities of the AH Coordinator. Whether the COB will function properly depends on its responsibilities and role in the full process being carefully delineated by the County Council; board members from the Maui community bringing a diverse set of competencies to the decision process; and the board receiving sufficient dedicated county resources such that members are well informed about the factors and tradeoffs involved in developing a particular project within budget constraints.

The Hawai'i Agribusiness Development Corporation (ADC) provides an example of how such an oversight board can fail to perform. ADC programs and its management are overseen by an unpaid community oversight board appointed by the Governor of Hawai'i. Two recent reports found serious, long-standing deficiencies in the operation of ADC programs, including a six-year period during which ADC did not make statutorily-required annual reports to the Hawai'i State Legislature or produce an accounting of its finances over the 2012-2020 period sufficient for the Office of the State Auditor to conduct an audit of its finances (La Croix and Mak, 2021; Office of the State Auditor, 2021). A well-functioning oversight board would have identified these problems and demanded that ADC management resolve them before new business was conducted.

Why did the oversight board fail to do its job? One reason was that the Board consisted primarily of high-ranking officials from other state government agencies who did not want to draw attention to a poorly performing state agency and stakeholders in agriculture who did not want funding disrupted to an agency serving their interests. After state legislators finally discovered the long-running problems, there were few repercussions for ADC board members or ADC's management. Two lessons from this episode could be drawn for the Maui Community Oversight Board (COB). First, it is important that the COB contain independent members drawn from outside county government and the broadly-defined affordable housing industry who understand that part of their job is to monitor whether the COB follows its statutory obligations and to take

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<sup>1</sup> The Plan proposes a \$70,000 salary for the Affordable Housing Coordinator. This is far below the salaries of department heads in Maui County. We note that low salaries in positions of high responsibility make it difficult to attract qualified people to the job, and increase the likelihood that the project development process will be tainted by corruption.

action when potential violations are discovered. The Plan mandates outside COB membership yet needs to ensure that these members have strong incentives to speak out when they see something wrong. Second, given the large amount of county resources—\$1.17 billion—to be made available to the COB, the ordinance establishing the COB should contain clear mechanisms by which the Mayor and Council monitor at regular intervals activities of the COB and Affordable Housing Coordinator.

It is important that the position of AH Coordinator and the Community Oversight Board (COB) be established such that they are consistent with the county charter. Creation of a new county department would require a charter amendment and delay implementation of the Plan, which already has a tight timeline. Regardless of whether charter amendments are necessary, it is vital that the coordinator be assigned sufficient power to resolve disputes across departments and to initiate proposals for investments from the Affordable Housing Fund and that the responsibilities of the Community Oversight Board be carefully delineated and monitored.

- **By-right development of 100% affordable housing projects through community decision-making and design standards that balance affordable housing while preserving valuable public health, cultural, and environmental resources. Update county processes to shorten the approval and development timeline and increase community-level decision-making for projects that will provide 100% affordable rentals and for sale homes and adhere to approved design guidelines. ... County and its contractor, Orion, should facilitate conversations with building industry professionals, nonprofits, and community members to further identify zoning reforms. Council should request a timeline, benchmarks, and reporting from the County on completion of zoning reform by 2023.**

This is the Plan's best feature. The change to "by-right" development of affordable housing projects is critically important because by-right design standards can achieve multiple objectives: (1) alleviate many community concerns about the development of affordable housing in their neighborhood by embedding minimum standards for affordable housing into the zoning code; (2) reduce the per unit cost of affordable housing by eliminating costly negotiations with neighboring communities and government officials that could result in costly project changes; and (3) shorten the time required to bring the units to market by streamlining the approval process.

Neighborhood residents often oppose affordable housing due to likely increases in traffic congestion and public school crowding as well as concerns about the impact of denser low-income housing on housing values, view lines, and neighborhood aesthetics. Opposition often takes the form of residents petitioning in neighborhood board or county council committee hearings for costly changes in the project's density, parking capacity, building heights and setbacks, and supporting infrastructure. The process of negotiating and obtaining approvals for changes in plans raises project costs and reduces projected project revenues by pushing out the time to project approval and completion. In many cases project developers abandon projects or never propose them in the first place because of the higher development costs and longer project timeline that the current approval process entails.<sup>2</sup>

In a by-right development process, a multi-family residential development is automatically approved when it complies with county zoning and land use regulations, meets a set of pre-approved design standards, and the developer/property owner has responded to input provided by the public at designated hearings.

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2 For a full description of by-right development approval processes, see National Multifamily Housing Council (2021).

Numerous cities and counties in California including Los Angeles County and the City of Santa Rosa have recently enacted by-right ordinances to speed up multi-family housing development. By-right development ordinances have the potential to speed project approval and substantially reduce project costs by reducing opportunities for neighborhood opponents of specific or all affordable housing projects to stop their development. For a by-right development system to work properly in Maui, there needs to be “buy-in” by the overall Maui community regarding the development of by-right procedures and standards as well as a community consensus on the need to build more affordable housing throughout the county. As the authors of the Plan state, this means developing “community decision-making and design standards that balance affordable housing while preserving valuable public health, cultural, and environmental resources” (p. 8). For community buy-in to happen, the Maui County government needs to fully vet with the public its proposed legislative package setting new procedures and standards for approving new affordable housing projects. Ultimately the new procedures and standards will need to be supported by a majority of the community, provide new procedures and timelines for community feedback on projects, and, most importantly, allow by-right development when the project meets predetermined design standards. The standards for development will need to have sufficient metrics of quality along multiple dimensions to attain broad community approval and yet not be so rigorous as to unduly raise the cost of affordable housing projects.

The Plan provides a mechanism for resolving disputes between communities and developers early in the planning process: “Developers should be required to meet with community advisory committees as many as four times to resolve issues surfaced by the community, but the design guidelines should mitigate most concerns” (p. 348). Other than the statement that “design guidelines should mitigate most concerns”, there is nothing in the Plan that explains why this four-meeting dispute resolution process will necessarily “mitigate” community concerns. Rather than just leave the purpose, and decision-making process for such meetings vague, the new by-right rules discussed above should include specific well-defined criteria and a high threshold for intervention in the proposed development, particularly for smaller projects. The community meeting should be limited to questions about whether the projects are consistent with project designs pre-approved by the County Council. If the meetings become forums wherein the development of affordable housing on the land parcel can be questioned, then the entire purpose of by-right development—the best feature of the Plan— will be defeated.

The by-right process outlined in the Plan suffers from one very important flaw: After the “community review and input process” has been completed and the project is found by the County to be “qualified for an exemption from the state environmental code (HRS Chapter 343),” opponents can still appeal (without resorting to litigation) the county government’s decision to the County Council. The Council could then reject the project and ask for changes. However, the whole point of by-right development is to replace the traditional discretionary approval process with a rule-based approach. The review of proposed developments should be entirely administrative, and a route of appeal to the County Council violates the central principle of the by-right system of affordable housing development. While the new review process for affordable housing projects is more streamlined and focused than the current system, the availability of a final appeal could lead to an affordable housing project being killed long after the Maui County Council approved a particular land parcel for affordable housing construction and considerable county resources and time have been spent planning the project and vetting it with the public. The availability of a final appeal could actually lead to fewer affordable housing projects being developed, particularly in communities where there is opposition to any and all affordable housing projects. For the by-right development process to function as intended, projects should be judged solely on the basis of the package of by-right rules set up in advance. The vetting of projects needs to occur at the start of project planning, when the County Council approves the land parcel for development



as affordable housing rather than just prior to construction. The Plan needs to be modified to drop the right of opponents to make a last-minute appeal to the County Council to stop an affordable housing project.

The Plan's proposal for by-right development of affordable housing projects focuses on public-sector development of new projects. However, once the County Council adopts new by-right procedures and standards, they should also lower costs to private property owners, non-profit developers, and for-profit developers to plan and obtain approval for affordable housing projects. The Plan should be modified to allow property owners to propose private development of affordable housing projects on designated parcels. Once the Council has approved use of these properties for affordable housing, the same by-right development procedures should be available to property owners and their developers.

- **Acquire and redevelop existing properties, when financially feasible, to create additional affordable housing opportunities.**

The Plan provides examples of other cities and counties that have directly acquired and redeveloped existing properties into affordable units, and suggests that the County of Maui may also want to acquire selected properties for redevelopment. An alternative to county acquisition and redevelopment of properties is for the county to provide a package of incentives to non-profit and for-profit developers and property owners to encourage redevelopment of small multi-unit properties. For this type of redevelopment, the choice of public versus private redevelopment should be guided by cost considerations, i.e., which process would yield redevelopment of these properties at the lowest cost to the public?

From 2019, the City and County of Honolulu has experimented with a program providing incentives to redevelopers, but the city government struggled to cope with procedural issues pertaining to program applications and saw very limited interest by property owners. The Honolulu City Council twice modified the program, with the latest revision passed in May 2021. The jury is still out on whether the program will be successful, but a recounting of how the program is structured and its missteps are discussed below, as the final restructuring could provide an alternative model for redevelopment of private properties on Maui.

In May 2019 the City and County of Honolulu passed and Mayor Caldwell signed Bill 7 which created a 5-year pilot program that provides incentives for owners of small (generally run-down) walk-up multifamily apartment buildings to remodel them as affordable housing units. The bill waives property taxes for 10 years; waives plan review and building permit charges, wastewater fees and park dedication fees; eliminates requirements for on-site parking, loading zones, and elevators; and allows higher heights and smaller setbacks on the lot. Building permits are to be issued within 90 days after their filing. In exchange, the apartment owner is required to lease 80 percent of the building's units to households at or below the Honolulu area median income at rents no more than those specified as affordable by the federal government. The rental restrictions are required to be in place for the life of the building.

Initially the program was a disaster. In its first 18 months, just nine property owners had applied for permits and only two had been approved.<sup>3</sup> Bureaucratic snafus plagued the program while many potential participants were put off by reporting requirements and the restrictions on unit rents for the life of the

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3 Janis L. Magin, "Honolulu incentives for affordable walk-up rentals get few takers." *Pacific Business News*, Dec. 2, 2020. Available at: <https://www.bizjournals.com/pacific/news/2020/12/02/honolulu-law-affordable-walkups-few-takers.html> (last access on 23 August 2021).

building. In response, in June 2020 the Council passed and Mayor Caldwell signed Bill 60 which limits the affordable rental restrictions to 15 years. The reduced rental restrictions led to two permits and 13 more applications in process by March 2021 but these results were well below expectations of the program's backers.<sup>4</sup> In April 2021, the Council passed and Mayor Blangiardi signed Bill 1 which established a grant program providing subsidies of between \$9,000 and \$15,000 per dwelling unit for property owners participating in the program.

The Honolulu program shows the difficulty in setting the right incentives to achieve two goals: (1) Encourage private redevelopment of multi-family buildings and (2) keep the new units affordable. Restrictions on renting the units to lower-income households had to be limited to 15 years and a \$10 million grant program was added to induce participation by property owners. Whether the program yields sufficient participation from property owners is still to be seen. If it does, it will come with the advantage of the units being redeveloped and managed by private landlords. This compares with substantial capital costs incurred by Maui County to acquire and redevelop the building and additional costs for public agencies to manage and maintain the property.

- **Partner with a community development nonprofit to establish an accelerated home building program that increases the number of accessory dwelling units (ADUs), 'ohana units, and single-family homes made available to households below 100% AMI.**

This recommendation is quite general, and does not provide a mechanism for how this partnership will work. The underlying implication is that most developers are not interested in such small projects. What needs to be defined is the nature of the partnership to be formed between the county and the non-profit community developer. Will incentives be provided to the developer to construct ADUs and 'ohana units on certain types of properties? Will the County be waiving certain requirements for these units? Will it be providing subsidies? How will these properties be identified?

More fundamentally, this recommendation needs more analysis. If it is possible that more construction might be stimulated on properties with below-median value housing by adjusting some rules for ADU and 'ohana units, then a partnership with a community developer might be somewhat redundant. A review of the Maui Ordinance regulating ADU permitting and construction (Chapter 19.35 - ACCESSORY DWELLINGS) reveals that ADU development is already by-right and entails relatively few additional rules beyond adherence to the county building code and existence of adequate sewer and fire road capacity. Alternatively, if a lack of interest by property owners traces back to difficulties in the owner obtaining financing or navigating the county rules for these types of development, then the Plan's recommendations for increasing assistance from non-profit financial advisors to lower- and middle-income households could be sufficient to incent additional ADU and 'ohana unit development. Finally, the County might consider using some of its \$58 million in tax revenues dedicated to affordable housing development to provide grants to lower- and middle-income property owners (up to 120% AMI) to build ADUs and 'ohana units on their properties.

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4 See Letter from Dean Uchida, Director, Honolulu Dept of Planning and Permitting, to Honorable Esther Kia'aina, Chair and Members Committee on Housing and the Economy, Honolulu City Council. March 25, 2021. Available at: <https://hnlldoc.ehawaii.gov/hnlldoc/document-download?id=10305> (last access on 23 August 2021).

- **Will increases in two types of property taxes be sufficient to finance the Plan?**

The MCCAHA Plan proposes to spend \$1.17 billion on housing and infrastructure construction, rental subsidies, and mortgage subsidies over the next 25 years. The plan is financed by (1) substantial increases in property taxes on nonowner-occupied homes valued at over \$3 million and short-term vacation rentals; (2) phasing “out apartment district properties allowed to be used for short-term occupancy at resale and permit and tax them as short-term vacation rentals with revenue dedicated to the Affordable Housing Fund” (p. 28). The increase in property tax revenues would serve as security for county revenue bonds used to finance construction of affordable housing units and housing infrastructure within the project’s first five years and make ongoing contributions to Maui County’s Affordable Housing Fund.

In FY2022 (July 1, 2021- June 30, 2022) the County of Maui projects that it will raise \$375.4 million in real property tax revenues with 62.2 percent of revenues coming from short-term rental properties (\$137.9 million) and non-owner-occupied residential properties (\$95.7 million) (County of Maui, 2021b). The FY22 tax rate (per \$1,000 of assessed valuation) for non-owner-occupied residential properties is \$5.45 for properties worth up to \$800,000 (Tier 1), \$6.05 for properties worth between \$800,000 and \$1.5 million (Tier 2), and \$7.50 for properties worth more than \$1.5 million (Tier 3). The Plan does not propose a schedule of tax hikes for the non-owner-occupied residential property tax category. Doubling the tax rates on Tier 2 and 3 properties would yield a maximum of \$40.2 million annually, while raising the tax rate on Tier 2 properties by 50 percent (\$6.03 million) and on Tier 3 properties by 75 percent (\$21.12 million) would raise a maximum of \$27.2 million annually. For simplicity, these calculations assume constant Maui housing prices and that the higher property taxes do not prompt property owners to take actions to change the property’s tax classification. The possibility that higher property tax rates will lead to tax evasion schemes should provide a cautionary note to policymakers: Large increases in tax rates can have unintended consequences that limit revenues to be raised from the tax increase. Finally, it is important to note that property tax rate increases on Tier 2 and Tier 3 non-owner-occupied housing could lead to higher housing costs for the middle- and higher-income Maui County residents who rent these properties. One must ask why middle-income and higher-income renters should pay higher rents to finance the new affordable housing project, while middle-income and higher-income residents who live in and own their homes continue to pay the county’s lowest property taxes and do not contribute to the cost of the new affordable housing units?

The Plan does not provide a schedule of its proposed tax hikes for short-term vacation properties. The FY2022 tax rate for short-term rental properties is \$10.70 for properties worth up to \$800,000 (Tier 1), \$10.85 for properties worth between \$800,000 and \$1.5 million (Tier 2), and \$11.00 for properties worth more than \$1.5 million (Tier 3). Raising the tax rates on Tier 2 and 3 properties by 50 percent would yield a maximum of \$24.1 million annually with the same assumptions and caveats mentioned above.

The Plan proposes to gain additional property tax revenues by reclassifying the tax category of apartments whenever they are sold, moving them from the low-tax short-term apartment-type rentals category to a vacation rental property tax category. Would this change yield much revenue? Suppose that all owners of properties classified as short-term apartment-type rentals immediately sold their properties. Their new property tax category—short-term vacation rental property—would raise their annual property tax bill by 95 percent, yielding an additional \$1.86 million annually for the county’s Affordable Housing Fund. Owners of these properties are, however, likely to sell them more slowly over a much longer time frame. With cumulative sales amounting to 10% of units in the first year and accumulating to 50% of units over a decade, new annual tax revenues raised from this reclassification would gradually increase from roughly \$0.2 million to roughly \$0.9 million over a decade. The bottom line is that this change in property tax classification is unlikely to fund more than 1-2% of the county’s annual expenditures on affordable housing.

- **Are there other taxation options that the County could use to finance the project?**

Are there other taxation options that could be used to finance the project? One possibility might be to use some of the revenues from the county's new Transient Accommodations Tax (TAT). In Spring 2021 a new state law eliminated state sharing of TAT revenues with the counties. In exchange, it allowed the counties to enact their own transient accommodation taxes of up to 3 percent. In October 2021 the Maui County Council enacted and the Mayor signed a bill establishing the Maui TAT at 3 percent, effective November 1, 2021. While Mayor Victorino has warned that the new county TAT may not fully replace the lost TAT revenues previously shared by the state (\$23 million in 2019), some simple calculations suggest that once pandemic conditions ease, the new tax may generate more revenue than expected. According to the HTA's 2020 Visitor Plant study, Maui County had 22,009 visitor accommodations, of which 6,235 were Vacation Rental units (VRUs). According to the HTA July Vacation Rental Performance report, Maui County VRU supply for July was a little more than 223,000 nights, or more than 7,500 VRUs (if every unit is available all 31 nights). Assuming an occupancy rate of 75 percent and an average daily room rate of \$400 for hotel rooms and \$250 for perhaps 7,000 VRUs, a 3 percent TAT increment would yield \$66.2 million in annual TAT revenues. Obviously, these results are subject to an easing of pandemic conditions and have a wide band of uncertainty. Nonetheless they serve to illustrate that over the next few years the new 3 percent county TAT increment could well generate substantial revenues, beyond the lost \$23 million previously shared by the State of Hawai'i, to support Plan expenditures.

- **Assess private developers of other residential properties for the off-site infrastructure costs applicable to their and other properties.**

One exemplary feature of the MCCAHA Plan is that it proposes (p. 28) that the county "take a more active role in developing the community serving infrastructure needed to support housing development." The Plan recommends that "the county develop this infrastructure rather than making it a requirement of the developer." This would allow developers to focus their efforts and financing on planning and construction of the affordable housing projects. The assumed logic is that by easing the burdens of large-scale financing borne by developers, more low-cost housing projects would be feasible. In turn, the County finances infrastructure from funds raised by revenue bond sales backed by increases in non-resident-owner residential properties and transient vacation rental property taxes.

However, the Plan states that off-site infrastructure would ultimately be paid for by imposing "a fee structure on market rate units that would recoup most, if not all, of the funds invested in infrastructure over time" (p. 28, 33). Such a fee structure could be warranted if the new infrastructure confers a large increase in value for market rate units. If, however, some of the off-site infrastructure is specific to the affordable housing projects, then a portion of the fees imposed on the private developer essentially represent a tax on private residential development. In other words, the Plan proposes raising the cost of market-oriented housing to lower the cost of affordable housing. This results in a smaller supply of all residential housing, and acts to offset some of the benefits of the additional supply of affordable housing produced by the County under the Affordable Housing Plan. Financing off-site infrastructure from the two property tax increases outlined in the Plan or from new TAT revenues would be less likely to negatively affect the overall supply of market housing built on Maui.



- **Sell bonds to fund the Affordable Housing Fund so the county has access to up to \$1.169 billion for implementing the plan over the next five years.**

Fall 2021 is probably the ideal time for the County of Maui to sell revenue or general obligation bonds to investors. Market interest rates on long-term municipal bonds in October 2021 are close to historic lows. In July 2021 the Maui County government sold \$84.75 million in general obligation bonds at a borrowing rate of 1.747 percent, and Moody's Investors Service assigned a bond rating to Maui County of Aa1 with a stable outlook. The real interest rate, i.e., the market interest rate adjusted for expected inflation, on Maui's recently-issued municipal bonds is negative, an extremely advantageous situation for a county borrower. We caution that market interest rates on municipal bonds have potential to rise considerably over the next few years if inflation risks are resolved with higher inflation over the next 18 or so months or if seasonally-adjusted visitor flows to Maui fall back substantially from the high levels seen from February to August 2021.

Given the timelines envisioned in the MCCAHA Plan, municipal bond sales would only be possible after the County Council and Mayor approve tax increases sufficient to finance new revenue bonds and approve changes in county procedures and standards affecting affordable housing. Under the Plan's timeline, changes in property taxation would be in place for FY2023 (which starts on July 1, 2022) and changes in county standards and procedures governing affordable housing projects would be finalized by the end of CY2022 or early in 2023. This ambitious timeline would enable a county revenue bond issue at some point in CY2023.

The Maui County Charter (2021) places restrictions on the type of expenditures financed by revenues raised from bond sales. Section 9-7 restricts the use of bond revenues to "bond retirement" and "capital programs". Thus, the Charter could restrict the use of revenues from bond sales to expenditures on the county's investments in construction of affordable housing and complementary infrastructure. This amounts to \$380 million over the life of the Plan (p. 10).

- **Assess and invest in community-serving infrastructure in all priority project areas.**

The MCCAHA Plan provides a general outline of complementary infrastructure projects. Beyond the initial planning stage for these projects, other Maui County departments that specialize in transportation or water infrastructure provision would likely be the agencies with the most experience in this area and with requisite experience to monitor contractors and expedite resolution of the many problems that often arise with public infrastructure projects. Some of these infrastructure projects, such as the new wastewater plant, have been discussed for more than a decade. The proposed changes in property tax rates provide a vehicle for their initial financing. The wastewater and water projects need environmental impact statements; much depends on how much planning has already been done for these projects.

- **The current workforce housing ordinance requiring 20% of the units produced in a development to be affordable will not meet the need when 54% of the units need to serve lower income households. Rather than requiring developers to produce 20% of their total units in a development as affordable housing, the plan recommends that 20% of the land be set-aside for affordable housing development. It is recommended the county use that land to produce housing at a higher density than the underlying zoning by using the 2.97 process so many more units than the current 20% policy are developed.**

The rationale behind this recommendation is straightforward: The county will develop the 20% of a market project's land with much higher density housing than the developer would otherwise choose. This

would increase the supply of affordable housing units beyond that which would be created by current requirement for 20% of the units in a development to be affordable.

We have several concerns that justify dropping or completely rethinking this recommendation. First, exactions on developers will lead developers to build a smaller overall quantity of housing than they would in the absence of exactions. The current requirement, that 20 percent of units in market-oriented developments be affordable units, has worked poorly, generating only small flows of new affordable housing. There is little reason to believe that a 20 percent taking of developer land will work better. Despite providing incentives for denser development of affordable housing units, the new requirement will still constrain the overall supply of new housing, and could lead to less affordable housing construction than is intended.

Second, the requirement that 20% of land be given up at the entitlement process will undoubtedly slow the entitlement process. Not all land on a parcel is equally valuable or buildable. The developer offering the 20% of land which is high cost to develop would not work but neither would the County taking the 20% of land which is most highly valued.

Third, the proposed new requirement raises an important question: is the proposed exaction a bigger or smaller taking than the previous developer exaction? It depends on the foregone premium when a unit must be sold as affordable and how many units fall into this category. It would be useful to understand how the size of the proposed exaction compares to the size of the current exaction.

Finally, it is possible that a land exaction would be challenged in federal court as an unconstitutional taking that violates both the Fifth and Fourteenth Amendments to the U.S. Constitution. Over the last 25 years, the U.S. Supreme has made four important decisions that limit the taking of land or imposition of fees as a requirement to develop land. While the rulings are focused more on county administrative decisions than on rules for development enacted by a state legislature or county council, the scope of U.S. Supreme Court rulings in this field has expanded over the last 34 years.<sup>5</sup> The bottom line is that a taking of 20 percent of a developer's land could trigger protracted state and federal litigation that could hold up the launch of Maui's program.<sup>6</sup>

- **Enforce fair housing and fair lending laws to ensure tenants' and homebuyers rights', including access to loan programs of their choice for mortgage prequalification and permanent financing and levy fines for violations of these federal laws with resources to support the Affordable Housing Fund.**

This is a well-founded proposal that has potential to improve access by some low-income groups to both housing and financing. For Maui to enforce these federal laws and to collect fines, it is vital that the County

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5 See *Nollan v. California Coastal Commission*, 483 U.S. 825 (1987); *Lucas v. South Carolina Coastal Commission*, 505 U.S. 1003 (1992); *Dolan v. City of Tigard*, 512 U.S. 374 (1994); and *Koontz v. St. Johns River Water Management District*, 570 U.S. 595 (2013). Much would depend on whether the Court views the land exaction as a proportional exaction to accomplish the County's affordable housing goal. The U.S. Supreme Court currently has a strong conservative majority, and could be inclined to rule against an affordable housing law that requires a developer to turn over without compensation some of its land in order to receive permission to build on land zoned for urban use. No one knows how the U.S. Supreme Court might rule but this provision raises the risk of lengthy litigation in federal and state courts.

6 Litigation within the state court system could hold-up approval of affordable housing projects slated to be built on state-owned lands that need to be reclassified to urban use. If opponents contest the State Land Use Commission's (LUC) reclassification of the land, then a contested case hearing would be held. LUC decisions are often appealed in state courts which can lead to additional LUC hearings and long delays in project approval.

enact fair housing and lending laws with provisions that parallel their federal statutory counterparts. When counties and states:

“have a fair housing law that HUD deems to be ‘substantially equivalent’ to federal fair housing law, the agencies charged with enforcing these laws may request certification from HUD. HUD directs complaints that it receives to these certified agencies and these groups can also be eligible for federal funding for enforcement efforts under the Federal Fair Housing Assistance Program (FHAP). In order to be certified, local or state agencies must enforce a fair housing law with substantive protections equal to or greater than the federal Fair Housing Act and follow certain minimum procedural standards. These include providing rights, procedures, remedies, and the availability of judicial review. Agencies must, for example, comply with rules establishing procedures and timelines for investigating complaints within 100 days and, when investigations exceed 100 days, provide a written statement explaining the reasons. HUD certification lasts five years” (Local Housing Solutions, 2021).

We caution that reliance on fines from violation of fair housing and fair lending laws to provide substantial funding to the County’s Affordable Housing Fund is a risky proposition. The main rationale for the County to establish and enforce fair housing and fair lending laws should not be to raise revenue but rather to set standards that provide more opportunities for minorities and low-income households in a community. Finally, we urge Maui County not to go it alone in this area. Litigation on fair housing and lending violations is a complex matter that often involves thorny matters of law and complicated expert reports. Cooperation between the four county attorneys, the state attorney general and the federal attorney in enforcing these laws would ease what otherwise would be a big burden on the Dept. of the Prosecuting Attorney for Maui County.

- **State Funding for Rental and Mortgage Subsidies. Provide IDAs paired with HUD housing counseling through new Affordable Renter and First-Time Homebuyer Programs to reduce upfront costs on local renters and homebuyers to obtain existing homes.**

The Plan states (p. 23) that \$789 million in housing support via rental housing development (\$489 million) and deferred payment mortgage subsidies (\$228 million) be made available to Maui families with household incomes below 120% of the Maui median.<sup>7</sup>

Mortgage subsidies include first-time homebuyer gap financing and deferred payment mortgages. The Plan is unclear about whether the down payment subsidies are repaid at resale and how interest is assessed, if at all. The Plan states that “[g]enerally, funds provided will not include interest. If interest is charged, the rate will not exceed two percent per annum for homeownership properties and three percent per annum for rental properties. All payments will be deferred until sale or refinance.” Such low caps might be reasonable in the context of 30-year mortgage interest rates that are just above 3 percent but could become outdated quickly if inflation increases over the next few years and interest rates rise proportionately. A better formula tying the cap to market interest rates and imposing an overall cap would ensure that neither borrowers nor the county suffer windfall gains or losses from changes in long-term interest rates.

It is unclear who owns, maintains, and manages the rental housing that is developed. Is the developer being contracted just to build the units or does the developer keep a management and ownership role after the project is built? If not, which county department has responsibility to manage and maintain the project?

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<sup>7</sup> The Plan also includes \$57 million over 5 years for “pilot and demonstration projects”, and \$15 million for “planning, design, engineering, and construction management for affordable projects.”

The Plan states that all affordable units developed under the Plan will be kept affordable in perpetuity. However, U.S. and state law tends to be hostile to the dedication of specific assets to particular uses in perpetuity. Values and the best uses of some of these lands could change dramatically over a 30-year time frame. Redevelopment into other uses could well be warranted at some point in the future and be strongly supported by future communities of Maui voters. Most fundamentally, dedication of assets to perpetual uses makes the strong and questionable assumption that the present generation has a better ability to make important decisions regarding their future use than future generations.

Some contingency for redevelopment and replacement of the affordable housing after a fixed number of years should be included in the legislation used to approve use of the land for affordable housing development.

- **Explore the development of a manufactured housing plant and locally sourced materials to increase the county's self-sufficiency and reduce the rising costs of building materials.**

The MCCAHA Plan's proposal to source building materials locally would be impractical and raise project costs. In 2021, the only lumber mills in Hawai'i are small operations specializing in processing hardwoods for niche furniture and decorative markets or in processing trees cut down by private and public property owners in their maintenance or development of properties. If the use of local lumber became a requirement of affordable housing projects, it would raise rather than reduce affordable housing unit costs. This is because manufacturing finished products in Hawai'i is usually more costly than buying them from mainland U.S. or foreign markets. Even if Hawai'i firms were to become competitive in producing raw and processed materials, this would not necessarily reduce costs of building materials to Hawai'i housing developers as the Hawai'i and U.S. mainland markets are closely linked. Lower prices in Hawai'i would trigger exports to the U.S. mainland and/or foreign markets, and raise prices in Hawai'i to near U.S. levels. Finally, there is likely to be little benefit to the county or even the state from becoming self-sufficient in processed building materials. The Plan's authors do not provide a rationale for why such a goal should be part of the Plan or why its incorporation would result in an increased supply of affordable housing.

The Plan's authors urge that the Maui County government explore the development of a manufactured housing plant but fail to mention that one already exists on the island of Hawai'i. HPM Building Supply, located in Kea'au, Hawai'i, produces HalePlus homes, which are "factory-built, modular, and transportable". The modular home part of HPM's business is still young, born out of a need for quick affordable housing after the destruction of 700 homes in the Puna District during the 2018 eruption of Kilauea. Clearly the existence of this pioneering Big Island firm shows that there is potential for a bigger local manufactured housing industry to emerge. Additional demand from Maui County and other counties for modular housing could lead to an expansion of HalePlus or to other local firms deciding to manufacture modular housing in Hawai'i.

More fundamentally, if there are substantial cost savings from using factory-built modular components in affordable housing projects, those opportunities should be pursued regardless of whether the components can be produced in Hawai'i. Several firms, including Impresa Modular and Honsador, import modular housing components and full modular homes from the U.S. mainland. The County of Hawai'i has already used factory-built modular housing built on the Big Island in its provision of shelters for evacuees of the 2018 eruption of Kilauea Volcano.



## CONCLUSION

The MCCAHA Plan provides a roadmap for the development of affordable housing in Maui over the next decade. Some central features of the plan need to be adjusted if the supply of affordable housing in Maui is to be rapidly increased. The Plan does a good job of outlining the scope of the problem and identifies new procedures and standards for the County to adopt to streamline its planning, approval, and construction processes. The shift to by-right development for multi-family projects is the most critical feature of the plan. Although the current version of by-right development presented in the Plan is flawed, the process can be easily improved by eliminating the final right of opponents to appeal the project to the County Council. The Plan identifies a potential source of tax revenue—\$58 million in annual revenues from increases in property taxes on two classes of property—that could be utilized to finance \$1.17 billion in expenditures over a 25-year period. Other sources of revenue are potentially available, including revenues from the county's new transient accommodation tax (TAT).

The Plan presents an ambitious public program for vetting, planning and developing affordable housing. The Plan's centralization of provision of affordable units in the public sector needs, however, to be supplemented by components of the plan that would allow by-right development of affordable units by private property owners and developers. The Plan's provisions for redevelopment of multi-family units by property owners, for by-right development of new multi-family projects by private developers, and development of ADUs and 'ohana units by low- and middle-income property owners need to be strengthened. And it is important to consider limiting the 20% land tax that replaces the existing 20% inclusionary zoning requirement and the proposed infrastructure fee to be imposed on developers of market rate housing for the cost of infrastructure serving both market and affordable housing. Both of these elements of the Plan will act to limit the total supply of housing in Maui County. With changes to a few key provisions, the Plan could lead to a big increase in production of affordable housing on Maui. The Plan is a big step forward, and the Maui County Council should move to adopt an amended version as its blueprint for this sector over the next decade.

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