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Perspectives

Reforming Homeowner Primacy and Improving Housing Affordability

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Volume 49, Number 7 - April 2, 2025 • Written by: Mr. Brett Pelletier, CRE

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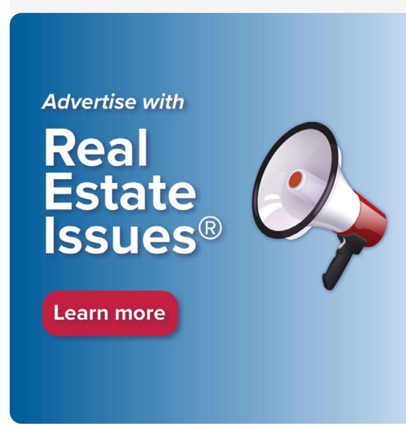

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Abstract

Housing is an issue of national and international importance. Its cost, its availability, its quality, and its standing as the bellwether for prosperity and success for individuals and economies. There is a housing crisis in the United States and affordable housing is complex and complicated. A variety of strategies, some simple, some not, are available to increase the supply of housing and decrease its cost. This article supports these statements with local

insights about local problems and solutions from Rhode Island. The only way forward is innovation and thoughtful strategic resource deployment that are targeted and followed up on. All housing is good housing, and everyone is a steward of the natural and built environments. Participants must constantly communicate and engage with the community, where there are many opportunities to balance the scales of equity, inclusion, dignity, respect, and kindness.

Introduction

Shareholder primacy, the corporate finance and management theory, asserts that the responsibility of management is to maximize the value for shareholders. Shareholder primacy dictates that business decisions are evaluated based on the impact on shareholder value, without consideration to stakeholders such as employees, customers, or the community. Much like shareholder primacy in the corporate finance context, this phenomenon exists and is observable in the local land use context and can be similarly described as "homeowner primacy". The parallels are striking, and the results have been discussed and studied intensely. This article discusses how homeowner primacy limits new housing supply and highlights solutions to addressing housing affordability, availability, and attainability. Affordability describes the level of rent or housing price to the income of a household, while availability describes the relative abundance of housing in a community. Attainable housing is not universally defined, but it generally describes nonsubsidized housing that is affordable to residents of a community, along the housing spectrum, typically with incomes between 80% and 120% of the area median income (AMI).

Housing continues to be top of mind for many Americans, real estate professionals and laypeople alike. Its cost, its availability, its quality, and its standing as the bellwether for prosperity and success for individuals and economies. It is so inextricably connected to the powerful concept of home. For many people in the United States and elsewhere, this conversation is less about the eccentricities of market cycles and the peculiarities of supply and demand imbalances, and more about the impact of those theoretical realities have on their lives and the lives of their families, friends, and constituents. Because it hurts.

When things hurt, there must be a problem and when there is a problem, there must be a solution. For many, the solution is just out of reach. That is why it feels like a crisis. The housing crisis feels different to people because it hurts…a lot. The American Dream is just out of reach for so many people. Prosperity eludes.

There are various discrete and combined market influences that impact housing cost and therefore its availability and accessibility within any community. Each of these 'levers' can be further refined, described, and elaborated on in order to identify ways to influence housing development and production. This high-level exercise centers on a five-step analytical approach to problem-solving that starts with 1) identifying the problem to be solved, 2) isolating the individual influences on the problem, 3) explaining the problem (to a larger audience), 4) connecting the problem to common issues and communities, and then 5) developing corrective action.

This article is not meant to be a comprehensive discussion of housing affordability and availability, or the influences on same. It is rather a starting point for developers, financiers, policymakers, and other participants in the housing value chain, to discuss strategies and empower solutions for exercising control or affecting change over each of the levers. This article proposes that there are seven primary levers that can be manipulated to influence the cost of housing and therefore the level of affordability and availability in development and delivery. Apply pressure to any of these levers and housing can be made more affordable to build and attain.

Identifying the Problem to Be Solved

As a real estate problem solver, it is essential to approach each assignment or scenario with a curiosity about what the problem is that needs to be solved. It is surprising how often this basic question is skipped in the early stages of work. It is a foundational step into the process. It needs asking. Otherwise, the problem cannot be solved. It becomes a thought experiment, absent a trajectory for action.

Housing is a problem in the United States. That, in itself, is not news, nor is it particularly specific or helpful in understanding the complexity and nuance of the issue. There is a supercharged public discourse being had around housing in this country and it impacts every single person, all the time. If real estate represents the intersection of the natural and built environments, and it does, then it touches every part of daily life. Real estate is the roads, bridges, and infrastructure improvements that get people to where they need to go, the office buildings

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where people work, the retail stores where they shop, the schools where they learn, the hospitals where they are cared for, and the homes where they rest, raise families, and establish community.

Throughout this article, affordable (little a) and Affordable (big A) housing will be used to describe two different things. "Little a" affordable housing is meant to refer to the general concept of housing that is affordable to a particular population, while "big A" Affordable housing is used to refer to regulated, more-or-less permanently affordable housing that is restricted to a specific population or income set-aside. Think apartments developed under the Low-Income Housing Tax Credit Program (LIHTC), deed-restricted condominium units for residents earning less than 100% of the Area Median Income (AMI), or Permanent Supportive Housing (PSH) for formerly chronically homeless households, among other flavors of housing products.

Not that long ago, political candidates spoke little of affordable housing, journalists wrote about all things except affordable housing, policymakers had nothing of affordable housing to debate, and regular people were not talking about affordable housing at the dinner table or over drinks. Those days are gone. In the 2024-25 Counselors of Real Estate Top Ten Issues Affecting Real Estate, housing affordability and attainability ranked sixth. Housing, in various forms, has appeared in the top ten list for each of the past eight years. So, what exactly is the problem, what are the underlying causes, and what tools or solutions are available to make progress in reducing the pain? It is worth remembering that this is a complex problem, and complex problems need complex solutions. None of this is simple and a grave disservice is done to others when the impression is given that it is.

Isolating the Individual Influences on the Problem

People in the Affordable housing business love acronyms. HTIA, is one term to add to the list. It stands for "housing that is affordable". The term is used as a way to speak about the character of housing that most people can agree on. People want to live in housing that is affordable.

It sounds simple, but it is worth stressing. It connects everyone. HTIA is a good economic thing, it is a good social thing, it is a good thing period. HTIA makes for better communities and makes for better economies where everyone benefits and thrives. There are plenty of case studies and graduate dissertations from housing and land economists who speak to the veracity of this assertion with metrics and models. For the purposes of this article it is an underlying assumption given that it is widely agreed upon and not a controversial statement at all.

Local market data on household income and housing costs illustrate dynamics of the problem relating to housing affordability and availability. Each of these problems are defined and described in the context of proposed solutions or innovations which are further described in this article.

Affordable Housing is a Market Failure

Regulated and restricted Affordable housing is what economists refer to as a market failure. Market failures exist when the market does not allocate enough resources to solve a particular problem in society. Simple examples of market failures are playgrounds, libraries, or fire departments. There is demand in the market for playgrounds, libraries, and the services provided by fire departments.

What is not likely to be seen in the market is a pay-for-service model of those cases because there is perhaps neither the ability nor the willingness for individuals to pay for those services. There is no market solution because the market will not allocate resources to create a playground, which requires an investment of both capital and operating expense from an owner or operator, without the ability to service that expense through an offsetting source of revenue. Charging toddlers a few dollars each time they use the swing set does not make for a good business proposition and illustrates the concept of a market failure, and the necessity of governments or other charitable organizations to step in. The same is true of Affordable housing. There is no market solution to house everyone in the United States at every income level.

In Rhode Island, for example, according to the 2024 Housing Fact Book, created and published by HousingWorks RI @ RWU (HousingWorks), the median household income is $81,370 per year, the median home price is $425,000, and the average two-bedroom rent is $2,107. Keep those numbers close at hand. HousingWorks concludes that a household would need $84,280 in annual income to afford an average two-bedroom rental unit in the state. If a household earned less than the median, they would experience more limited capacity and availability in the housing market, and owning a home is unlikely to be possible because the estimated income needed to afford a median-priced home is $143,687. At below the median income, where half of all households fall, rent or monthly ownership expenses would need to be less than $2,000 per month to be affordable and attainable to that cohort of households. The market will not provide a solution to build new construction units to house those households because rents and prices that low would never justify the cost of construction and operation. With construction costs and capital markets in their current state, rents need to be much higher than $2,000 per month in order to justify the cost of construction of new apartment units in Rhode Island.

Explaining the Problem

For years, it was taken for granted that if a household had an income at or above the median, then that household was more or less taken care of by the market and public policy need not worry much about those households. They had choice in housing, they could buy or rent in the market with access to abundant options that were affordable to them. That is no longer true. If a household earns the median and can no longer afford market-rate housing, the number of households that require some intervention in order to make the housing market work for them must expand.

That means, in the Housing Fact Book data referenced above, half of the households in the state of Rhode Island could not afford to go into the market and buy or rent at the median. They cannot afford market-rate housing. Therefore, there is no market solution to their housing problem. The market is not allocating resources to serve that population, and the market is not providing a solution to housing for those households. That is a market failure. This can be observed in many markets across the country and with many income cohorts along the spectrum. Housing affordability impacts everyone.

There are a huge number of influences on housing costs in the United States, some more impactful than others, and some more controllable than others, with significant variance from jurisdiction to jurisdiction. Geography and political jurisdiction matter for property taxes, builders, liability, and hazard insurance. Utility costs vary, snow removal in the north, air conditioning costs in the south, and on and on. However, more fundamentally, lack of supply is foundational to any conversation about housing. If limits are put on the supply, and demand grows, a freshman with half a semester of economics would rightly conclude that prices will go up, and up, and up.

Supply Shortages Abound

Housing is expensive, for a number of reasons. Lack of supply pushes prices up, because more people want fewer available goods, which means that those with the means to pay more, can and do. There are increased regulatory costs, cost of construction materials and labor, inflation, rising interest rates, and huge property insurance increases, all contributing to relatively more expensive housing, well exceeding wage growth. The one thing that is true is that in order to make housing more affordable, the cost must be reduced or otherwise offset with subsidy. If it costs $425,000 to build a home, then developers and governments can reduce the overall cost, or pay for it with free or cheap money in the form of low interest loans, grants, and low-cost equity, in order to make it more affordable to people who can only afford, say, a $200,000 home. This is especially important in markets where there are no $200,000 homes. This reality has had a growing impact on conversations around zoning and land use reform.

According to the National Low Income Housing Coalition (NLIHC), there is a shortage of some 7.3 million homes for extremely low-income renters in the United States. Extremely low-income households are typically defined as those who earn less than 30% of the Area Median Income (AMI). Think of AMI as a statistical median income for all households in a jurisdiction. If a household earns 100% of AMI, they earn the statistical median, in Rhode Island that is around $81,370, which means at 30% of AMI, that number looks more like $24,411.

In Rhode Island, NLIHC reports that 69% of these vulnerable households pay more than 30% of their income for rent and an astonishing 56% of households pay more than 50% of their income on rent, making it nearly impossible for them to afford other necessities such as transportation, food, education, and healthcare. Forget saving for a down payment.

Rhode Island has always been a pretty expensive place to live, but for a number of reasons it has become much more so lately. There are just too few homes. One of the things Rhode Island is doing is exploring ways to have a major impact on housing supply. That includes a state initiative to study a more active and direct role in the development of Affordable housing in the state through a state-controlled public development entity, similar to the

Housing Opportunities Commission of Montgomery County, Maryland. When people are revisiting public ownership models and reigniting a conversation about the state and federal government's role in building and owning housing, that is remarkable.

Another innovation that Rhode Island has pioneered is the creation and staffing of a Proactive Development entity, lead by Ben Frost as President. Ben is a true housing advocate, policymaker, and thought leader who is serious about contributing to solving the housing crisis in Rhode Island. Proactive Development works with government agencies, municipalities, developers and the public to grow housing production across the state. Serious housing people need to roll up their sleeves and get stuck into the messy work that is untangling, repairing, and rebuilding systems. Rhode Island is doing just that.

This is an international challenge and there are a lot of lessons that can be learned from others' collective experience. Every tool in the toolbox is needed, especially in times of inflationary pressure and regulatory uncertainty. High, and rising, insurance costs are a topic of conversation in commercial real estate circles, and it is something that has an outsized impact on Affordable housing because of the regulated and restricted income potential in relation to the operating costs. If it costs more to build and operate a unit of housing, fewer units of housing can be added to supply for the same amount of investment. Insurance and operating cost pressures are issues housing professionals in Rhode Island are intimately aware of.

Connecting the Problem to Common Issues and Communities

Each of these problems (lack of supply, affordability, escalating development and operating costs) is foundational to understanding just how complex and complicated the housing question is, and how the problem needs to be analyzed, and solutions crafted. Each lever, on both the supply side and the demand side, should be analyzed to determine what opportunities exist for influence and what strategies are necessary for change.

It is generally true that the cost of housing is made up of three main parts: the cost of the land, the cost of building construction, and the cost of ongoing property operations once complete. There are seven primary levers that directly impact the cost and availability of housing in most markets. Each of these levers can be pulled or pushed to influence the cost of housing and therefore the level of availability, affordability and ultimate development and delivery. The three main cost centers of land, construction, and operations have subgroups with individual line items that need focus, and each participant in the housing value chain has an opportunity to influence one or more of those subgroups, especially policymakers.

1. **Land and Infrastructure** are significant initial cost centers, and the availability of land is a barrier to development. A lower land cost means a lower per-unit development cost, so if it is possible to reduce the cost of land, by increasing the density of the site through density bonuses, value capture subsidies, or subsidized infrastructure costs, housing becomes more affordable to produce. If the development is the beneficiary of low or no-cost land, the project costs will be lower, and housing becomes more financially feasible to develop. Allowing greater density on smaller-sized lots is a powerful tool in unlocking value that allows developers to make a deal pencil, where it previously might not have.
2. **Entitlements and Regulation** typically includes the many permits and legal and regulatory hurdles that need to be met in order to build housing, and they can vary significantly with geography and jurisdiction. Expedited permitting, approvals, and planning review can result in lower costs and shorter timelines, which reduce risk and ultimately expense. Reliability and predictably of comprehensive permitting processes are a benefit to this exercise and pave the way for risk reduction in entitlements. Rhode Island is looking to reform its standardized local real estate tax treatment for Affordable housing developments, locally known as the 8% Law.
3. **Hard Construction Costs** include raw materials, site work, labor and all the generally understood costs to build housing units. Strategies that can reduce overall cost to develop include value engineering, lower-cost materials, and innovative building technologies like 3D printing, modular and panelized construction, manufactured housing and adaptive reuse of existing buildings. In Affordable housing, these initial capital costs may put downward pressure on financial feasibility because the increase on hard costs may not be offset by an equal or greater benefit. However, they are well worth pursuing. Underwriting may be slow to catch up to these innovations and must realize the future operating expense gains and sustainability which impacts long-term affordability.
4. **Soft Costs** include engineering, architecture, permitting, design, legal, financing, and various construction insurance costs. These individual costs have an impact on overall cost and affordability as well. These costs

are more marginal to an overall project budget, but every bit counts. Cost savings can include repeatable models, simplified designs, and replicable, simple products. Creative thinking around insurance coverage is the most recent soft cost that needs attention. Captive insurance companies, risk pools, and Joint Ownership Entities are all tools gaining attention nationally.

5. Limiting the **Profit** a developer can generate from a project in order to accommodate affordable housing, workforce housing, or other community benefits is a noble compromise. Nonprofit project sponsors can often deliver lower-cost housing because they limit overhead and profit extracted from the deal. Limited dividend policies for developers who utilize public financing, or other taxpayer-funded subsidies can reduce the total development cost of a housing unit and reduce the future costs through limits on equity cash out. Smaller numbers, every little bit counts. This is where the conversation of public ownership models gains most traction.
6. **Future Operations** include all the operating expenses a property will be subject to once built. Expenses like sewer and water can be reduced by greywater recycling systems, and domestic water management systems, solar arrays and wind energy can reduce electricity expenses, Passive House and Net Zero construction can reduce heat loss and utility bills. Reducing utility expenses make the property cheaper to operate which translates into profitability and ability to support debt, reducing the need to additional gap filling subsidy. Further, arrangements with the government can reduce property taxes to help subsidize the creation of new housing for residents who cannot afford market housing.
7. **Capital Sources and Financing** that deploy subsidized interest rates and low or no cost capital provide significant upside benefits to the construction of rental and for-sale housing. Low and no cost land, expedited permitting, and reduction of project timing reduce the capital outlay needed and the finance carrying costs that these projects are required to support. LIHTC, grant funds, Federal and State agency loan products, and revolving loan funds for debt and equity placement are all worth considering in addressing these issues.

Each of these levers are opportunities to influence the cost of housing and therefore the level of availability, affordability, and attainability. Increased programming and funding for affordable housing programs can be done at the federal, state, and local levels by increasing subsidies for affordable housing developers, providing tax incentives to encourage the development of affordable housing and increasing funding for housing vouchers and other rental assistance programs. At the local and state level, reducing regulatory barriers and streamlining the development process will help alleviate the crisis in a significant way. Many local zoning laws and building codes make it difficult and expensive to build, which reduces supply and increases pricing. Good for those owners who are already there, but bad for everyone that wants in. By reducing these barriers, it can become easier and more cost-effective for developers to build more housing, which enhances communities, economies, and most importantly…people’s lives.

Enter one of the fundamental barriers to making change. Vested interest in nothing changing. Shareholder primacy is a concept in corporate finance and management that asserts that the primary responsibility of a company’s management, including executives and boards of directors, is to maximize the value for shareholders of the company, often, and infamously, no matter the cost. This approach holds that the main goal of a company is to increase the financial returns for its shareholders, most commonly resulting in stock price increases and to a lesser extent in modern times, dividend payments. Under shareholder primacy, business and financing decisions are evaluated primarily based on their impact on shareholder value, sometimes at the expense of other stakeholders such as employees, customers, and the community. This principle is often associated with a more recent view of corporate responsibility, where the interests of shareholders are considered paramount, as described in the Friedman doctrine.

There are a number of examples from recent history that illustrate the imbalance that this philosophy can cause, such as the Eastman Kodak Company, Sears, Roebuck, and Co., Enron, and the list goes on. Of particular note is the case of the Eastman Kodak Company, a company so wedded to the philosophical imperative of shareholder primacy, that it was almost their complete undoing. In 1975, when one of their employees invented and attempted to develop and market the digital camera, leadership of the company was resistant to moving away from their core film business, which would require investment in new technologies and risk to shareholder value and steady profits. That risk was too much to bear for management and shareholders, and the result was that Kodak missed out on piloting one of the most powerful technological rocket ships in the modern era. Protection of the existing and exiting shareholders took precedent over anything else, and it nearly cost them everything.

Developing Corrective Action

In contrast to shareholder primacy, there are other governance models that emphasize balancing the interests of various stakeholders, including employees, customers, suppliers, and the broader community, not just shareholders. This approach is sometimes referred to as stakeholder theory or corporate social responsibility (CSR). The general theory has presented itself in a number of catchy titles over the years. Post-Enron, some business curriculums began to pay closer attention to adjacent stakeholders. Employees who lost their jobs or retirement savings, or both, residents of the host communities, local governments who pay a price for exiting firms or uses through reduced tax base, jobs, flow-through economic benefits, and on and on. The parallels that are easily observable in local and state land-use decisions, and therefore, as a result, housing policy are remarkable.

For nearly 100 years, or since the 1926 landmark U.S. Supreme Court ruling on Village of Euclid v. Ambler Realty Co., many local governments have allowed, and in fact encouraged a priority on home value protection (increases) to the benefit of existing homeowners over just about everything else in making local housing policy and land-use decisions, development, planning, and zoning. This serves to enhance the economic benefits of existing homeowners and exiting homeowners (sellers), to the detriment of nearly every other population cohort within or adjacent to a community. This is backed up by some frustrating, yet unsurprising research completed in 2023 and published by Lydia Lo, Owen Noble, and Yonah Freemark with the Urban Institute. The research resulted in a report titled 'Who Makes Planning Choices', that describes how lopsided the participation is in the land-use planning and decision-making process at the local level. Renters, young people, workers, newcomers, employees, women, people of color, and other marginalized populations are often an afterthought, if a thought at all. That has had significant detrimental impact on outcomes for many of those populations, to the benefit of, among others, existing homeowners.

Like shareholder primacy, in its sole focus on one stakeholder at the expense of the bigger picture, this phenomenon can be similarly described as homeowner primacy. The parallels are striking, and the results have been discussed and studied intensely. A key externality of homeowner primacy is the downward pressure on new housing supply. Not enough homes have been built for the number of people who need to live in a particular community. This is especially true in the Northeast, and especially true in Rhode Island where only 9% of the land area in the state is zoned for more than three residential units, and only 8% of the land area in the state is zoned for more than four residential units, by right.

Increasing supply is foundational to correcting the supply and demand imbalance, which will certainly have an impact on pricing. Local zoning reforms will need deployment in order to make it easier to build. Absent that, the strategies focus on reducing costs of what can be built. The two main strategies to address this situation include the technological innovation route of creating homes that are cheaper to build through modular construction, manufactured methods, tiny homes, and 3D-printed homes, to name a few. The other is to deploy capital through equity and debt investments that offset those development or operating costs, such as the LIHTC program, Section 8-style mobile and project-based housing vouchers, or lower-cost capital from CDFIs and the like that serve to subsidize the creation of HTIA.

Just like the problems with shareholder primacy prompted the response of other governance models that emphasize a more balanced interest approach with either stakeholder theory or corporate social responsibility (CSR), there exists the opportunity to apply the same logic to homeownership primacy. There needs to be a land-use policy reform that considers the true meaning of community real estate development that pays closer attention to adjacent stakeholders, including renters that are ignored by public representation, would-be residents priced out of communities without a voice, employers who struggle to fill positions and grow economies because housing has become unaffordable. Breaking the cycle of homeownership primacy with some variant of CSR is a fundamental policy shift that would unlock the rest of the levers.

Conclusion

Housing is complicated and deserves attention and serious conversation, and not just among housing advocates, developers, and policymakers. But in this moment, return to the discussion of market failures, and the price governments and citizens pay for some other mechanism rather than the private market providing the necessary good or service. These solutions come with a cost and are typically in the form of taxes, subsidies, and other soft grants. They cost taxpayers. That is absolutely true. What is often forgotten or ignored in the conversation is the benefit that society receives in exchange for that expenditure. What the taxpayer does is provide treatment for a societal ill, and if not curing it entirely, reducing the hurt felt by neighbors, friends, and family.

It is worth reiterating that all housing is good housing and there is a renewed interest for increasing density, availability, and affordability, from everywhere. That interest and energy is only valuable if it is productive. It is important that all stakeholders pay attention to conversations about community and engage in them. Everyone is a steward of the natural and built environments and therefore must constantly communicate and engage with the community, and there are many opportunities to balance the scales of equity, inclusion, dignity, respect, and kindness.

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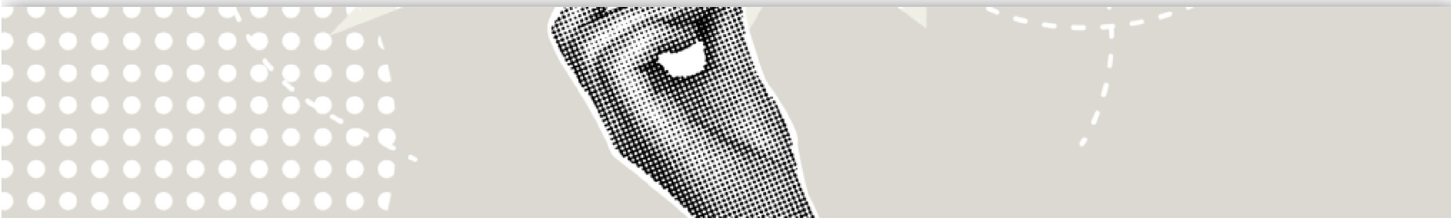

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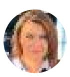

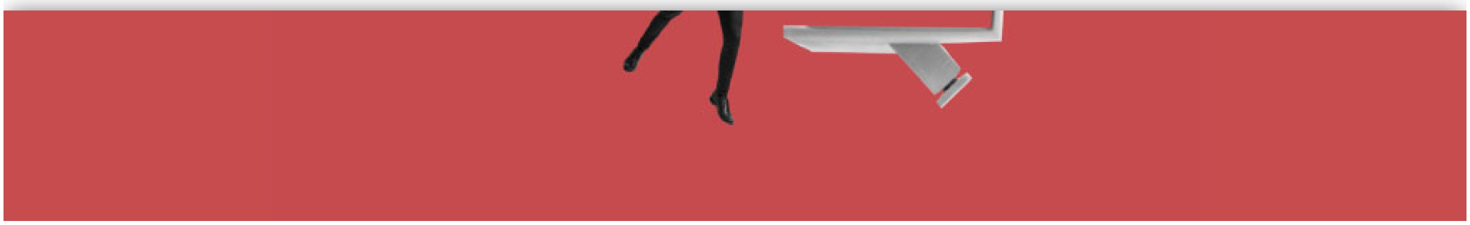

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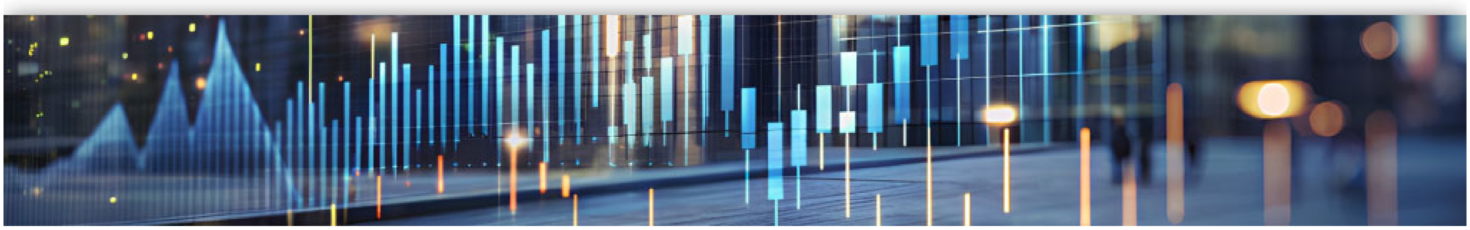

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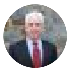

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