



Before FHA was created in 1934, residential-commercial districts were quite common. Traditional streets composed of a mix of commercial and housing - i.e., Main Streets - were common partly because lenders appreciated that risk was spread over different types of real estate. For example, a flower shop with an apartment above provided two sources of income. One might perform well when the other was not. But now lenders look at traditional districts as adding risk - "one use or the other could fail so better not to allow it at all." As a result, the signal to investors and developers is if you want financing, avoid residential-commercial districts and stick to single-use.

Despite this regulatory stance, in recent years the desire for traditional districts has steadily gained popularity. We know this not so much from new development, but rather from the demographic trends that show attraction to existing urban and suburban places with housing, retail and commercial property in close proximity.

New development has not served this demand partly because of federal policies and practices that discourage such settlement. Specifically FHA, Fannie Mae, Freddie Mac, and HUD's 221d4 and 220 programs all limit non-residential to a small percentage of the total value or imputed rent of a given project. (Fannie Mae currently sets the cap at 20%; Freddie Mac at 25%; and HUD's 221d4 and 220 programs at 15% and 30%, respectively.) Combined with the tendency of private lenders to adopt even more restrictive policies than federal underwriting rules, this excludes almost all of America's pre-World War II Main Streets, as well as newer forms such as live/work units, from the secondary mortgage markets and from HUD's capital program for rental housing.

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In the article, "The Next One Hundred Million," University of Utah professor Arthur C. Nelson estimates that the current supply of unattached single-family housing already exceeds projected demand and will continue to do so until 2037. Further analysis by Nelson (see "Reshaping America's Built Environment") indicates that as the glut of large-lot homes continues to flood the market, an emerging demand for smaller housing in walkable, traditional neighborhood settings is on the rise. The demand for *housing types* has changed in the marketplace, but current government policies obstruct developers from meeting public demand. To remove obstacles to investment in these economic times, the government should heed market demand and allow a mix of commercial and housing development to act as a catalyst for economic growth.

Alix Rice, VP of development for Atlanta-based Green Street Properties, has dealt with the repercussions of FHA-created impediments directly. Green Street's Glenwood Park - a traditional community development made up of single-family homes, townhouses, condominiums, and commercial retail across 28 acres about two miles from downtown Atlanta - was nearing completion of their successful residential-commercial development when the final plans for incorporating eight condominium buildings and an

additional one-story retail building were stopped. Although the proposed retail building would serve the entire community and not just the eight condo buildings in which it was bundled together with on the underwriting application, FHA rejected financing completion of the project as the one-story retail building pushed the retail component of their development towards 35%, deeming the successful project ineligible under current regulations. As Rice said, "we are suffering for the way we structured our condo association, and now, willing buyers are eager to move, but cannot get financing because we are non-FHA approved."

Federal regulations currently hamper market recovery by assigning risk by *type of development*, disfavoring mixed-use areas that have performed better during the current housing crisis. The worst performing and riskiest investments – single-use, sprawled-out areas at the metropolitan edge - are still preferentially classified. Oddly, the federal remedy to the housing crisis has been to assign risk to one of the few segments of the housing market in which demand is growing.

The net effect of all this is that:

- 1. Obstacles to investment prevent market-driven traditional neighborhood districts, which considerable evidence shows consumers choose.**
- 2. Investors and developers are discouraged from developing walkable and environmentally sustainable communities that meet growing market demand.**
- 3. US housing and banking policy conflicts with the HUD/DOT/EPA Sustainability Partnership that seeks to improve the environmental and economic performance of the US economy.**

CNU suggests that HUD and Treasury relax or eliminate restrictions on housing adjacent or attached to non-residential development. Risk should be assigned based on credit worthiness, not by the government's dictate that separate-use zoning reduces risk, when clearly it does not. Such reform will:

- 1. Allow investors and developers to produce the communities people are looking to place their families and their dollars.**
- 2. Enable investors and developers to create and capture value in building out financially and environmentally sustainable communities.**
- 3. Align government policies to accomplish stated federal goals and priorities, leveraging public investment in infrastructure improvements.**

As Christopher Leinberger has written, "Housing is such a large part of the economy that a sustained, robust recovery is difficult to imagine without a corresponding recovery in the building, buying, and selling of houses." Working with our partners at Association Information Services, Inc., the Community Association Institute, the Center for Neighborhood Technology (CNT), the National Association of Home Builders (NAHB), the National Association of Realtors, and the National Town Builders Association (NTBA), the Congress for the New Urbanism has advocated for FHA, Fannie Mae, Freddie Mac, and 221d4 to raise and/or eliminate the restrictive covenants on commercial space in traditional neighborhood districts. By recognizing the latent demand hindered by the current restrictions in place, FHA, HUD, Fannie and Freddie have an opportunity to not only support smart-growth policies attuned to the goals of the HUD/USDOT/EPA Sustainability Partnership, but also help jumpstart much-needed economic growth.

**Reform FHA, Fannie Mae and Freddie Mac to allow investment to respond to market demand.**

**For more information, see [www.cnu.org/fanniireform](http://www.cnu.org/fanniireform)**