

LAND VALUE RETURN

TOOLS TO FINANCE OUR URBAN FUTURE

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In an era of tight budgets and exploding need, cities around the world are funding infrastructure and other public improvements through land value return, also known as land value capture. This policy approach offers an array of public finance tools that enable communities to recover and reinvest land value increases resulting from public investment and other government actions. Notably, as new subway lines, roads, and other public works raise the value of nearby land and real estate, developers and property owners share that publicly generated windfall to help local governments pay for new bridges, transit, parks, affordable housing, and other infrastructure upgrades.

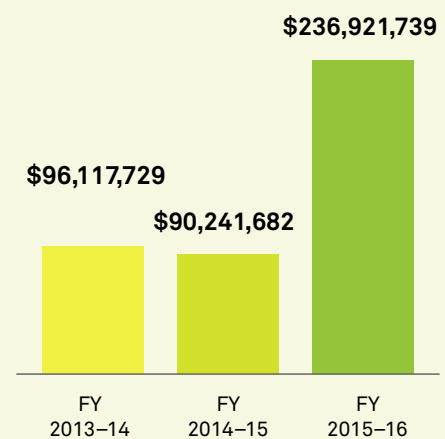
Land value return is based on a simple core premise: public action should generate public benefit. As challenges mount from rapid urbanization, deteriorating infrastructure, climate change, and more, this funding source has never been more important to the future of municipalities.

Land value return enables communities to recover and reinvest land value increases resulting from public investment and other government actions.

When used in conjunction with good governance and urban planning principles, land value return can be an integral tool to help governments advance positive fiscal, social, and environmental outcomes. On every continent, communities are already improving quality of life for their residents through such instruments, which include: betterment contributions, charges for building rights, inclusionary housing and zoning, linkage or impact fees (figure 1), special assessments, transferable development rights, and even certain applications of the property tax (pages 2–3).

Figure 1

Revenue from Development Impact Fees in San Francisco, California, 2013–2016



For decades, the City of San Francisco, California, has levied impact fees—monetary exactions charged to a developer as a condition of approval for a development project. Those revenues finance the cost of public infrastructure improvements necessitated by a new development, helping to manage growth as more residents utilize municipal transportation networks, parks, and other assets. The fees collected from fiscal year 2013 through 2016, for example, funded transit needs, bicycle infrastructure, pedestrian capital improvements, and more.

Source: City of San Francisco, FY2014–15 & FY2015–16 Biennial Development Impact Fee Report.



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The Land Value Return Toolbox

In practice, land value return includes a range of mechanisms and policies, which various jurisdictions implement and practice differently. All of these tools share one common goal, however: returning land value to the public. Several examples follow.

TOOL	JURISDICTIONAL EXAMPLE
<p>Betterment Contributions and Special Assessments</p> <p>Owners of select properties pay the municipality a fee, which defrays the cost of a public improvement or service from which the owner specifically benefits.</p>	<p>City of Manizales, Colombia</p> <p>Betterment levies from property owners have contributed to the city's revenue base for urban infrastructure financing and funded road improvements, urban renewal, and the renovation of notable projects such as the Alfonso Lopez Plaza.¹</p>
<p>Charges for Building Rights</p> <p>Developers pay the municipality a fee for additional development rights, which funds infrastructure or other public improvements.² In some jurisdictions, developers can bid to purchase building rights in the form of higher floor area ratio (FAR) from the city at auction.</p>	<p>City of São Paulo, Brazil</p> <p>CEPACs (Certificates of Additional Construction Potential in Portuguese) are a form of charges for building rights that are sold on a securities exchange. The city has generated nearly US\$2 billion from CEPACs to fund infrastructure and planning programs within a designated redevelopment area.³</p>
<p>Exactions</p> <p>Developers pay the municipality (in cash, land, or other in-kind avenues) to obtain special approvals or permissions required to develop or build on a parcel, in order to defray the cost of additional public services required by new development.</p>	<p>City of Córdoba, Argentina</p> <p>Articles 180–188 of the city's provincial constitution impose this mandated charge on developers who seek changes in existing building norms.⁴</p>
<p>Impact Fees (Linkage Fees)</p> <p>Developers pay the municipality a one-time charge designed to cover the costs associated with a development's impact on certain public services and infrastructure, and the municipality invests this revenue in public services and infrastructure.</p>	<p>Orange County, Florida, United States</p> <p>Impact fees generate funds for parks, fire stations, police cruisers, and other public safety investments.⁵</p>

PROPERTY TAX AND TAX INCREMENT FINANCE (TIF)

Property taxes can be an important form of land value return, as well-functioning property tax systems base obligations on the market value of real estate. But that link is not automatic. Rather, it depends on the enabling and administrative frameworks in place for the property tax. Land value increases in jurisdictions with well-functioning property tax systems should generate higher assessed values for properties near planned public investments—and such taxation does return some value to the public from private entities for the public sector. However, limits on

value assessments or increases can restrict the property tax's ability to succeed as intended.

Many communities use tax increment finance (TIF) to promote economic development and community investment by earmarking property tax revenues from anticipated increases in assessed values within a designated district. Because TIF directs the use of existing property taxes, some observers may erroneously believe that it is a tool of land value return. In fact, it is more properly a device that transfers value from one area to another rather than one that returns additional value to the public sector.

TOOL	JURISDICTIONAL EXAMPLE
<p>Inclusionary Housing or Inclusionary Zoning</p> <p>Developers provide the municipality with a certain amount of low- or moderate-income housing in exchange for the right to construct market-rate residential or commercial properties.</p>	<p>City of Cambridge, Massachusetts, United States</p> <p>Via its 1998 Inclusionary Zoning Ordinance, the city created 1,000 units of affordable rental and ownership housing in new developments located throughout the city.⁶</p>
<p>Land Readjustment</p> <p>Landowners collectively cooperate with a municipality or developer to pool their land to accomplish a redevelopment project. The investments in infrastructure and services undertaken on the pooled land are intended to increase the value of the properties in the redeveloped area; afterward, each landowner receives a smaller parcel of land that has greater value due to the improvements made.</p>	<p>Greater Tokyo Capital Area, Japan</p> <p>In one of the most successful examples of large-scale redevelopment in the 20th century, the Greater Tokyo Railway Network used land readjustment as a strategic component of its financing.⁷</p>
<p>Rail Plus Property Co-Development (R+P)</p> <p>In the area where a new rail line will be built, the government transfers land development rights to a transit authority at the before-transit development price. The authority then partners with private developers to further develop properties near the new transit route, shares the profits, and uses the funds to reinvest in the rail system and other public improvements.⁸</p>	<p>Hong Kong, China</p> <p>The Hong Kong Mass Transit Railway (MTR) Corporation has used the R+P model for three decades to build vibrant neighborhoods, conserve open space, and construct a railway system that covers 221 kilometers and serves more than five million people. The Corporation has at times raised US\$1.5 billion annually via the self-sustaining R+P model.⁹</p>
<p>Transfer of Development Rights</p> <p>Landowners pay a government entity a fee to transfer the density potential (as established in the local zoning law or ordinance) of one tract of land to a noncontiguous parcel of land that is better suited to greater densities. The fee generates revenue for public investment, and the transfer of density can also further urban planning objectives.</p>	<p>Pennsylvania, United States</p> <p>The state uses the transfer of development rights to permanently protect farms and natural resources by redirecting development from such areas to parts of municipalities meant to better accommodate development. This furthers conservation objectives and produces revenues that municipalities can use for public investments.¹⁰</p>

¹ Luis Schloeter, "Financing Urban Infrastructure in Emerging Cities: Betterment Levies," *Ciudades Sostenibles* (blog), Banco Interamericano de Desarrollo, January 8, 2016, <https://blogs.iadb.org/ciudadessostenibles/2016/01/08/betterment-levies/>.

² Martim O. Smolka, *Implementing Value Capture in Latin America: Policies and Tools for Urban Development* (Cambridge, MA: Lincoln Institute of Land Policy, 2013), 35–37.

³ Gregory K. Ingram and Yu-Hung Hong, eds., *Municipal Revenues and Land Policies* (Cambridge, MA: Lincoln Institute of Land Policy, 2012), 218–219; Leão Serva, "How São Paulo Uses 'Value Capture' to Raise Billions for Infrastructure," *Citiscopes.org*, May 22, 2014, <http://archive.citiscopes.org/story/2014/how-sao-paulo-uses-value-capture-raise-billions-infrastructure>; CEPACs can also be purchased in a secondary market where developers can sell them among each other.

⁴ Smolka, 34.

⁵ Stephen Hudak and Martin E. Comas, "Orange, Seminole Counties Boost Impact Fees to Keep Up with Growth Demands," *Orlando*

Sentinel, January 10, 2018, www.orlandosentinel.com/news/orange/os-orange-county-impact-fees-20180108-story.html.

⁶ "Inclusionary Housing Program for Developers," Community Development Department, City of Cambridge, accessed June 5, 2018, www.cambridgema.gov/CDD/housing/fordevelopersandpropmanagers/inclusionarydevelopers.

⁷ Gregory K. Ingram and Yu-Hung Hong, eds., *Value Capture and Land Policies* (Cambridge, MA: Lincoln Institute of Land Policy, 2012), 290–291.

⁸ Lincoln Leong, "The 'Rail plus Property' Model: Hong Kong's Successful Self-Financing Formula," McKinsey & Company, June 2016, <https://www.mckinsey.com/industries/capital-projects-and-infrastructure/our-insights/the-rail-plus-property-model>.

⁹ Leong.

¹⁰ "Transfer of Development Rights," *ConservationTools.org*, Pennsylvania Land Trust Association, accessed June 5, 2018, <https://conservationtools.org/guides/12-transfer-of-development-rights>.

Land Value Return in Practice

Government officials have long recognized the need to use land value to fund sustainable urban development, but the ability to mobilize land value return instruments often depends on factors including legal enabling authority, political will, fiscal frameworks, and the capacity of public officials. A few representative examples of land value return policies and the instruments they enable are below.

CHARGES FOR BUILDING RIGHTS

Enacted in the National Constitution of 1988, Brazil's Federal Law 10,257/2001 codified municipal charges on building rights and the use of CEPACs to help municipalities capitalize on rising land values.¹¹ It also allows the government to charge private developers for the right to develop land above a defined floor area ratio (FAR). These instruments encourage fair distribution of the costs and benefits of urbanization by allowing municipalities to leverage them according to local needs and contexts.

INCLUSIONARY HOUSING

In 2017, Denver, Colorado, began using land value return to create affordable housing in River North, a former industrial hub that is transforming into a mixed-use neighborhood anchored by a new commuter rail station. Using a zoning tool known as an “incentive overlay,” the city allows developers to construct taller buildings in exchange for creating affordable housing. More than a dozen projects are already in the pipeline; the city projects that hundreds of affordable homes will be built by 2022 thanks to the incentive overlay—effectively four times the number of affordable units constructed elsewhere in the city. Denver leaders plan to create additional overlays and to expand the land value return concept for affordable housing across the city, especially around transit stations and commercial corridors.

TRANSFER OF DEVELOPMENT RIGHTS

Building density in Mumbai, India, is limited by the floor space index (FSI)—the ratio of allowable floor space to the plot area. The city can then redirect development intensity by allowing property owners to sell or trade the rights to their unused FSI.¹² Mumbai also enables the sale of development rights, allowing developers to purchase up to a specific amount of additional FSI from the government, to generate public revenues to fund urban infrastructure.



An artist's rendering of the 2020 Zocalo Community Development in Denver's River North neighborhood. Credit: Craine Architecture, Inc.

Conclusion

A city's built environment is the result of cumulative land use decisions and investments. Infrastructure and buildings shape a city's character and urban form for generations, and land value return can significantly improve that process. In practice, successful implementation demands management of many complex factors and diverse stakeholders; proper understanding of land market conditions; comprehensive property-monitoring systems; fluid communication among fiscal, planning, and judicial entities; and political resolve to realize the full potential of land value return.

Our challenge now is to better understand the intersection of policies arising under different levels of government, within public authorities, or through special entities—any of which can create a foundation for the implementation of land value return.

Looking ahead, practitioners seeking strong urban outcomes should plan to learn from varied global experiences with the implementation of land value return policies and tools. We should also work to increase knowledge of the complex nature of various approaches, and to promote greater understanding among public officials and citizens about how these tools can benefit their communities—and our shared urban future. □

¹¹ For a history of *Outorga Onerosa do Direito de Construir*, which was established by Federal Law 10,257/2001, see Fernanda Furtado and Isabela Bacellar, “Public Charge and Private Transfer of Building Rights in Brazil: The Need for Coherence in Regulation and Implementation” (paper, IV World Planning Schools Congress, Rio de Janeiro, July 3–8, 2016).

¹² Marco Kamiya and Le-Yin Zhang, eds., *Finance for City Leaders*, 2nd ed. (Nairobi: UN-Habitat, 2017), 202.