Trends in land use and government policy affecting real estate development in the USA

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Abstract
Land use in the United States is shaped by a combination of direct regulation and financial incentives targeting development. The real estate industry is regulated at local, regional, state, and federal levels of government. While the most direct control is still exercised by local zoning authorities, policy is increasingly influenced by regional and state authorities, particularly in technical aspects of project design, but also when projects are likely to create substantial economic or fiscal impact. As regional impacts of land use have received greater scrutiny, state and federal authorities have responded with additional regulation and incentive structures, sometimes with unintended consequences. As local markets are increasingly shaped by larger forces, paradoxically much new development is established under the control of non-governmental associations, devolving operational regulation to the most local level of governance.

Finance for development has also been greatly affected by macro-economic forces, policy responses in the wake of the Great Financial Crisis of 2007–2009, and technological innovation. This chapter presents an overview of a number of recent changes affecting development finance, both on the private and public side. Programs such as the EB-5 Immigration Program, crowdfunding, and private equity funds are changing how developers raise equity. Public–private development is also evolving with increasing reliance on tax increment financing, community benefits agreements, linkages and exactions, business improvement districts and incentive zoning, and value recapture.

Introduction: Land use regulation and governance
Historically, the regulation of land use in the USA has been highly decentralized, with decision-making in the hands of local officials or boards charged with implementing county or municipal zoning and subdivision ordinances. Decisions, enforcement actions and new laws may be challenged in local, state, and federal courts, but these challenges typically involve procedural fairness or jurisdiction, rather than the underlying land use issues. Increasingly, policy preferences of regional, state, and federal governments have begun to more strongly influence the type, mix and design of development, even when these policies are enacted...
through local control processes. As land use policies grow more coordinated, a parallel devolution is occurring at the lower levels of governance, to extremely local non-governmental entities that have taken on functions associated with municipalities and counties.

**Zoning and related controls**

Local control of land use is most commonly implemented through municipal zoning, which directly enables allowable uses and densities on all parcels within a delineated zone. A typical designation, such as “R-4” indicates a residential zone allowing four units per acre, and is further defined in the ordinance to allow single-family homes, duplexes, for example, and offer conditional approval on potentially suitable uses, such as inns or small commercial use. Zoning usually includes basic dimensional requirements such as minimum setbacks from property lines and maximum building heights, and in jurisdictions with substantial development pressure the code may include exacting standards for semi-public elements such as signage and architectural features. Some rural jurisdictions do not have zoning, but where it exists, most land use decisions are simple determinations: Is the proposed use consistent with zoning? Conforming proposals may be approved administratively, by municipal or county planning staff as so-called “as-of-right” development.

**Re-zoning and land use change**

Land owners wishing to change use, or to increase density above the limit of their zone, may petition for re-zoning. In fact, changes to the existing zoning of land are a primary means by which land value is created in the USA. Owners may apply to change to another existing designation, or to alter the text of their zone in the law. As an example, a developer may buy a parcel in zone “R-10,” allowing homes on 20,000 square foot lots, and propose that the site is more appropriately developed as multi-family mid-rise housing. Amendments like these typically cannot be reviewed administratively, and open the project to public hearings, usually before a zoning board or planning commission. This path is more formal, requires comprehensive documentation and public notice, is more susceptible to opposition, and therefore riskier.

Whether administrative or political, most zoning ordinances require a set of cross-coordinating reviews by multiple officials. These reviews may direct comment to laws outside the zoning code, such as a water protection ordinance to minimize impact on shared community groundwater. They typically involve health, fire and safety officers, and public works engineers who review and comment on more technical aspects of a proposal such as sewer capacity, fire truck access, or stormwater management. These studies range from quick checks of road and septic facilities to comprehensive review of proposed construction procedures for managing impacts, depending on the jurisdiction and project complexity. Technical review of projects continues after zoning approval in the form of building permits. Building permits are required for substantial construction in most jurisdictions, and may require detailed submission of structural, mechanical, and electrical drawings, as well as coordinated civil engineering by state-licensed professionals. Increasingly, building codes require a certification of green building standards. The building permit process for a single family home is short, often requiring minimal documentation, while complex commercial buildings may take months to review, comment, and resubmit under statutory timelines.

Following the explosive growth of many American cities in the postwar period, many larger municipalities began more closely regulating land use, both by expanding the body of zoning
ordinances, and by adding new legal mandates and administrators. Large municipal planning departments may include a variety of specialized professionals addressing ordinances on affordable housing provision, fiscal, social-service, and environmental impacts of development proposals. As cities expanded outward into automobile-dependent suburbs, serious deficiencies were revealed in local control. First, ordinances intended to manage growth could be “leapfrogged” by moving beyond the jurisdiction, and second, the scale of development impacts might now extend to multiple jurisdictions, such as a city’s watersheds, road traffic, or school system. As a result, many municipalities have consolidated some kinds of land use control, at least in policy, to regional entities, which may maintain mapping and planning expertise, author resource and development plans, and review proposals on behalf of member communities (Fahmy, interview). These planning entities operate in an increasingly crowded landscape of regional actors in transportation, conservation, and energy planning, and are in many cases conduits of state and federal grant funding toward specific planning priorities. It is becoming common for substantial development projects to face some level of regional-plan review.

State regulation and enforcement

In some cases, the administrative burden of development, or the scope of identified impacts, is large enough to warrant state intervention in the process. This is often the case with state public health reviews of items such as septic systems or restaurant facilities, environmental impacts addressed by state law, or other aspects of a project regulated by state or multi-state standards, such as building or energy codes. In such cases, the local jurisdiction usually remains the coordinator of permitting activities, and refers the proposal to authorities as required. Environmental review of a proposed project is commonly managed by a state Department of Environmental Quality or similar agency, which is empowered by state law to enforce regulations on land use changes in a variety of sensitive natural resources. Developments which impede or alter streams, identified wildlife habitat, agricultural or historic resources or scenic views may be required to submit documentation to receive a specific approval or permit for each. The scope of these reviews has continually increased as citizen pressure, lobbying, and legal action have led to specific state laws to address agricultural and historic preservation, regional habitat protection, and other impacts (Kassell, interview). Increasing technical review of these standards has also opened new routes of legal challenge to unpopular development, as opponents may contest approvals they feel are insufficiently rigorous under the law. Projects open to these kinds of statewide reviews can expect substantial delay and costly professional fees to clear these hurdles.

State oversight of local land use processes

State interest in land use has expanded in recent decades to include issue-specific reviews of several issues relevant to developers. The Chesapeake Bay Preservation Act is Virginia’s legislative component of a larger multi-state agreement to protect coastal resources from upstream sedimentation and other pollution. To this end, state regulations can reach into local land use planning to improve development standards and comprehensive plans, and to regulate their enforcement. Other states such as Oregon and Maryland have adopted statewide smart growth laws that hold local codes and decisions to a standard for sustainable land use planning, to promote generally compact and walkable development. Some states favor carrots, offering substantial funding and expertise to local bodies who agree to update their zoning and related ordinances. These laws have had mixed success, as legislative initiative has usually run ahead of
funding and implementation. Nevertheless, regional, county, and city plans promising smart or sustainable growth are proliferating in US jurisdictions, and sometimes create tension between customary ways of doing business and actual rules. Issue-specific legislation may address housing, as in Massachusetts, where statewide inclusionary zoning rules were adopted to compel provision of lower-cost housing within approvals of new projects. For more than a generation, compulsory affordable housing percentages were a feature of large urban projects, but states have shifted with planning doctrine to promote more integrated types and costs of housing, even beyond city limits. Similarly, laws attempting to address climate change have been introduced in California, with potentially broad effects in real estate, where energy intensity is linked to density and transit choice (Fahmy, interview).

**Federal involvement in land use**

The mechanism for federal involvement in land use is similar, but follows a generation behind states. Federal oversight over impacts to waters of the US has been in place since the 1972 expansion of the Clean Water Act. Since then, scientific understanding of non-point source pollution and sedimentation has advanced to become a major concern in the preservation of watersheds, and land disturbance is, along with the filling of wetlands, the most common reason for direct federal permit oversight. The jurisdiction of this regulation has broadened consistently, and land uses need be only tenuously related to the hydrology of navigable waters to fall under jurisdiction of the Army Corps of Engineers (USACE) permit program. Cost and delay are often sufficient reason to alter designs to achieve lower-impact development patterns when crossing even minor streams or emergent wetlands. Again, the local zoning agency most often plays a coordinating role, but developers planning a substantial project must have a professional study the parcel to determine jurisdiction and prospects for approval. Other federal reviews can include the Department of Fish and Wildlife (DFW) and the Environmental Protection Agency (EPA), and the Department of Housing and Urban Development (HUD).

Most recently, federal interest in land use has appeared in explicit smart growth initiatives of the federal government. The Sustainable Communities Initiative, a partnership of HUD, EPA, and the Department of Transportation (DOT) has, since 2010, added additional conditions to their direction of infrastructure funding. Because federal highway funding is a major driver of cities, smart growth advocates have long complained that by underweighting urban populations’ per capita needs and emphasizing regional and interstate networks over mass transit, federal funding has been a driver of suburbanization and low-quality development choices, and the new initiatives attempt to direct both planning and hard construction to projects that promote a more compact, city-centric settlement pattern. Largely a product of the Obama administration, the longevity of these initiatives is uncertain, but if they persist, the effects of even a modest redirection of resources could be substantial for real estate in the USA. Many of the innovations and project types of the postwar American land use are fundamentally suburban in character, and increasing urbanization is requiring adjustment of concepts such as road standards, housing types, and retail concepts. If nascent trends toward urban living continue, and if infrastructure investments and other incentives align with trend, a substantial change in development may result.

**Changes in regulatory approach**

At every level, controls on land use have followed a trajectory of broadening scope and increasing scrutiny, but the implementation of these controls has followed what seems like an
opposite direction. In many relevant areas of regulation, local and state actors have changed their approach from prescriptive rules to performance-based standards. Simultaneously, enforcement, and sometimes even creation and maintenance of standards may be outsourced to third parties as communities attempt to regulate issues about which municipal officials have no particular expertise. These trends reflect tension between a new quantification of land and resource use in environmental design, and the necessary pullback of public employees as governments have limited overhead in the aftermath of financial crisis. “Quantification” in this case refers to the array of data sources such as Geographic Information Systems (GIS), which allow comprehensive mapping of resources, and also to the array of modeling tools, such as ComCheck, to facilitate closer calculation of development proposals’ actual impacts (Kellenberg, interview). Where laws might prohibit “deposition of fill within twenty feet of a stream bank,” a similar control today might refer to a publicly available GIS layer that delineates actual hydrology of a region and limits of Total Maximum Daily Load (TMDL) in a receiving watershed, referring to Best Management Practices (BMPS), promulgated by a society of engineers, which may be appropriate to achieve compliance. Such standards offer a dual benefit, allowing design flexibility to tailor solutions to projects, while offering a measurable compliance test.

The complexity of demonstrating compliance is, however, beyond the scope of most jurisdictions’ capability, so standards may be maintained as independent certifications that must be submitted by an engineer hired by the applicant. Third party certification belongs to a larger trend of government outsourcing, and may include soil and water evaluations, certification of septic or fire-protection design, hazard identification, even extending to more subjective reviews like compliance with architectural standards.

Energy codes and green buildings

The most complete example of this phenomenon is green building standards. For a generation, some level of green building has been a portfolio requirement of many government agencies and universities. Energy codes have been in place in California and some municipalities since the late 1970s, but just as interest in energy efficiency has come to public notice, prescriptive codes have given way to performance standards maintained by third parties (Kiefer, interview). Where energy codes were once fairly limited in scope, requiring, for example, minimum R–values in building envelopes and mandating that a percentage of fixtures be energy efficient, modern state or municipal codes may allow certification under GreenPoint, EnergyStar (a federal standard), or LEED (Leadership in Energy and Environmental Design) to a certain threshold and climate zone referenced by the standard. LEED is maintained and continuously updated to reflect building science and improving technology by its author, the US Green Building Council (USGBC). The result is a set of options that the designer may trade to find an affordable and achievable path to substantial reductions in resource use and other environmental criteria. Buildings and land developments can voluntarily contract with auditors to demonstrate compliance.

New zoning codes

The concept of flexibility in achieving a performance standard has reached even the basics of land use, where it seems a difficult fit with zoning’s reductive legal approach. Zoning is criticized (usually fairly) for presupposing the separation of use groups. In fact, the last major innovation in zoning was the postwar idea of the Planned Unit Development (PUD), which addressed this problem. PUDs allow a mixture of uses and building types to be co-developed under a master plan, typically on a large parcel, in ways that may not meet the zoning code, but
which provide a successful physical program for the site. In addition to mixed use developments, PUDs have been used for special-use facilities such as airports that simply don’t fit into use-based zoning. While an improvement, the PUD approach is still parcel-by-parcel. Many planners have long pointed out that the successful creation of urbanism relies on the comingling of mixed uses, on many parcels, to create streetscapes which perform diverse functions for owner/tenants, for vehicles, and for the pedestrian public. Related to smart growth, many architects and developers have successfully promoted alternative Form Based Codes (FBC). Rather than sharply segregating use, FBC codes presuppose mixed use in many locations, and may in fact refrain from specifying particular uses, other than to prohibit nuisance. Rather, the municipality (and this is usually an urban phenomenon) designs several prototypical street types, which are specified in form and pedestrian function (Plater-Zyberk, interview). These may be more or less appropriate to different locations in the district, and suitable for a variety of uses, but if the template is followed, all development will contribute to increasing key measures of quality.

Private infrastructure and governance

Coalescing land use and performance standards around new development have coincided with a 30-year boom in the creation of non-governmental entities performing functions long associated with municipal sovereignty. Some are large, with access to capital, and may provide privately funded infrastructure, as in a public–private tollway. More common is the smaller voluntary or semi-voluntary organization, such as the Downtown Improvement District or Home Owners Associations (HOA). In both cases, property owners enter agreements (which run with the property, not the owner) to provide funding, usually in the form of a regular assessment, which is aggregated and spent in common on community priorities. In Special Districts, this usually takes the form of a levy paid on area businesses or owners that might be used to fund streetscape improvements or other infrastructure serving the area.

In Homeowner Associations (HOAs), all owners of a residential community are liable for assessments to fund maintenance and programs for the community, including capital improvements to shared resources. The concept is not new, but its proliferation is impressive: Over 60 million Americans are members of some form of HOA. These organizations have always regulated and maintained planned communities and condominiums, but over the past 20 years they have diversified into a wide array of service provision. Telecommunications and other utility services are commonly contracted through the commons, and architectural review and dispute resolution are adjudicated. New, more walkable development models, such as those promoted by Smart Growth America and the Congress for a New Urbanism (CNU) are utterly dependent upon this community “software” to successfully manage the many shared common areas that make them appealing: plazas and parks, in-community school and other public facilities (Killore interview, 2010).

Governmental reaction to these private, hyper-local governance structures is of interest. They have risen in prominence as confidence in municipal service provision has, in many places, declined. They also relieve budget pressures. Where state and county road agencies once measured their success by miles of new road, maintenance of existing infrastructure is now the overriding concern (Kiefer interview). A strong preference for public roads meeting common standards, sometimes financed by private developers, but always dedicated to the system after construction, has in some cases reversed. Some highway departments relish the privatization of many of these “last mile” segments under community maintenance agreements. The reviewing agency may simply confirm that the maintenance agreement is binding and complete, and
count itself lucky not to have to do the job. Similarly, downtown businesses may relish the ability to complete streetscape improvements without taking the time to convince all the voters of a town to approve a bond with a narrow benefit.

**Policies affecting development finance**

**Debt**

Development in the United States has benefited from historically low interest rates since the Great Financial Crisis of 2007–2009. Traditionally, developers of income property have obtained a permanent mortgage commitment before they begin development of an apartment, office, retail, industrial, or other form of income property. They would then take the permanent mortgage commitment to a bank who would provide a short-term construction loan to construct the project and carry it through lease-up. When the project achieves stabilized occupancy or reaches pre-defined levels of net operating income (NOI), then the permanent mortgage will be funded and will ‘take out’ (pay off) the construction loan.

In the early 1980s, interest rates soared in the United States to double-digit levels and permanent mortgage commitments became very hard to get. At that time, developers obtained “mini-permanent” loans of 3–5 years. These “mini-perm” loans were used to construct the project and to carry it for several years of operations, with the expectation that interest rates would fall and more reasonable permanent mortgages would become available. Today, some of the largest developers will construct projects without permanent loan commitments, but smaller developers still require such commitments in order to obtain construction financing, since construction lenders are rightfully concerned that there will be a permanent loan take-out of their short-term financing.

Land development, condominiums, and other for-sale projects have no permanent loans. They are constructed using only short-term development loans or construction loans and are paid off as the lots or condominiums are sold. Unlike credit lines where the loans can be reborrowed, land and condominium loans have release provisions that stipulate the loan repayment or “release” amount as each sale is made. The releases are usually a multiple – 1.2 or 1.3 – times the pro-rata share of the loan (release price = value of lot sold/total value of land × maximum loan amount × multiple).

**Equity**

Equity requirements in most income properties range from 30–40 percent of the total cost. While small developers typically must raise equity from friends and family, larger developers with strong track records are able to access institutional sources. These include pension funds, private equity funds, family offices, insurance companies, endowments, and sovereign funds. Equity may also be available from publicly traded funds such as Real Estate Investment Trusts (REITs), but more often than not, REITs prefer to own the real estate rather than to joint-venture a project with a developer or sponsor. Institutional investors may be accessed through pension fund advisors and investment brokers.

Many developers will leverage their equity by borrowing mezzanine loans. Mezzanine loans typically occupy the second debt position and carry interest rates ranging from 10–12 percent or more, but they reduce the developer’s equity to 10–15 percent of the total capital cost. Ever since the Global Financial Crisis started in 2008, banks have been very cautious about making construction loans (Wang and Zhang, 2014). Many developers have found that construction
and development loan terms are so onerous or have such low loan-to-value ratios that they have sourced better terms borrowing from private loan funds like Mosaic Real Estate Investors who make 1–3 year first-mortgage loans to developers ranging in loan-to-value ratios from 60–75 percent with interest rates in the low teens.

**Private finance**

**How are developers raising equity today?**

Equity investment in real estate has changed dramatically since 1990. Private equity funds and REITs have been the dominant source of equity as shown in Figure 29.1. In the historically low interest rate environment that has persisted from 2009 to 2016, there has been an abundance of equity, but fewer high-quality investment opportunities. Private equity funds and foreign equity investors have poured money into US real estate, bidding prices up and cap rates down. While offering strong potential, crowdfunding remains in a state of “watchful waiting” (PwC and the Urban Land Institute, 2015).

Roy March (2012) highlights five major reasons for the explosion in new sources of equity and debt. The biggest catalyst for bringing in new capital sources was the Savings and Loan Crisis in the late 1980s and the formation of the Resolution Trust Corporation (RTC) to liquidate the assets of failed thrifts. “Seizing the opportunity to provide liquidity to an industry that had none, a handful of entrepreneurs, private equity firms, and Wall Street merchant banks formed the first so-called opportunity funds.” The RTC jump-started both the real estate private equity funds and the CMBS industries. A second factor was the growth of the equity REIT market which has soared from $5.5 billion in 1990 to $846 billion in 2014 (NAREIT,
2016). A third factor was the very low interest rates on mortgages and other investment alternatives that have spurred institutional investors, led by university endowments, notably Yale and Harvard, to increase their allocations to real estate, moving from core investments into more value-adding and opportunistic real estate investments. A fourth factor has been the deluge of cross-border investments due in large part to the emergence of sovereign wealth funds. The US remains the “safe haven” for investments, especially after the Great Financial Crisis of 2007–2009. Finally, the fifth factor has been the evolution of technological innovation, which has helped the industry overcome its reputation for lack of transparency. Public information has provided accurate and timely data and more democratic access to it. With the growth in REITs, more REIT analysts are covering the industry (see March, 2012).

As March notes, there is a dark side to this increase in equity capital. With real estate more closely tied to global financial markets, it is more closely correlated with other financial asset classes, reducing its appeal as a counter-cyclical alternative investment. Whereas prices used to be “sticky,” moving slowly relative to the stock market, the closer correlation has increased the volatility of real estate. This has made real estate investment riskier and less of a hedge for mitigating portfolio cyclical risk.

**EB-5 immigration program**

The EB-5 program provides foreign investors with the opportunity to obtain a green card if they invest $800,000–$1.2 million in a US business venture. The program has been a particularly popular source of equity for real estate, especially for Chinese investors. To get approval, developers must demonstrate they will create 10 jobs for each visa issued. The program is limited to 3000 visas per year for qualifying immigrants who invest in Targeted Employment Area (TEA) locales, while an additional 3000 visas per year are set aside for investors in a Regional Center project. The program has been used to raise equity in a number of high-profile projects including Hudson Yards ($600M) and Atlantic Yards ($475M) in NYC and Time Warner ($272.5M) in the Los Angeles Film Regional Center. EB-5 funds can be invested both in equity and debt. Investor return requirements are very low – 2–6 percent. Real estate is popular because of the perceived safety as an investment (Jahangiri, 2014; Savills Studley, 2015). The program is controversial because it allows foreign nationals to buy US green cards.

**Crowdfunding**

Crowdfunding – raising money over the internet – is in its infancy as of 2017, but promises to be an increasingly important source of equity. Made possible by the JOBS Act of 2012, real estate crowdfunding has grown from $0 to $.25 billion in 2015, with 131 crowdfunding platforms in the USA (Dong, 2016). In general, real estate crowdfunding allows investors to share in any financial returns or profits of a given investment. The JOBS Act effectively removes the Securities and Exchange Commission prohibition on general solicitation and advertising for private placement offerings. Originally limited to accredited investors, Title III of the JOBS Act enables small investors to invest in real estate with certain limitations – investors with net worth or annual income below $100,000 may not be sold more than $2000 or 5 percent of their net worth or annual income in any one year (Dong, 2016, p. 21). While some crowdfunding platforms vet each deal very carefully, other platforms simply provide a marketplace for investors and those looking for money to meet with little or no screening.

The crowdfunding industry has yet to experience an economic downturn. Since regulations have been considerably relaxed for non-accredited investors, many unsophisticated investors are
likely to find themselves in weak or overleveraged deals. When the downturn inevitably occurs, there will likely be a fallout in the industry and a series of lawsuits involving crowdfunding companies that have sponsored bad deals. Nevertheless, crowdfunding is here to stay and will be increasingly important over time.

**Private equity for land development**

Private equity funds have long concentrated on income property, but as the real estate cycle has matured in 2013–15, there has been increasing appetite for new development. Most of the investment has gone into land that is already entitled for development. However, lots for homebuilding have become harder to find in parts of the country, such as California and Texas, where the volume of homebuilding has been high. Some public homebuilders, such as Lennar and Toll Brothers, accumulated a sizeable land bank during the 2008–10 economic downturn, but others, such as D. R. Horton, the largest US homebuilder, and the Pulte Group, have a shorter inventory – 7.4 years versus 12 years. This trend to reduce inventory followed the disastrous experience of builders during the S&L crisis, where excessive land holdings caused many to face bankruptcy. Indeed, major homebuilders earned some of their highest profits on land entitlement and development during the 1980s, but when the market crashed, they could not afford to hold on to their land.

Development activity in the United Kingdom illustrates the build-up of development activity toward the end of the cycle. Figure 29.2 shows that the sales of development sites in London and the rest of the United Kingdom are well above their long-term average and in fact are back to their 2006–7 levels. Spain, by contrast, has lagged well behind the UK in its recovery following the Global Financial Crisis but the appetite for development is re-emerging.

![Development site sales well above average](image-url)

**Figure 29.2** United Kingdom development site sales back to 2006–7 levels

*Source: Real Capital Analytics, 2015*
Public–private development and public finance

This section describes several of the most popular programs for providing public financial assistance for economic development. While these programs were originally devised for urban renewal, they have become increasingly used for neighborhood stabilization and economic development undertaken by private developers.

Community Benefits Agreements

Community Benefits Agreements (CBAs) are legally enforceable contracts signed by community groups and a developer setting forth a range of community benefits that a developer agrees to provide in conjunction with a development project. They are intended to be negotiated directly between community groups and the developer. The developer agrees to provide specified community benefits in exchange for the community groups’ support of the proposed project for entitlements and approvals (Gross et al., 2002).

CBAs are related to development agreements, which are contracts between a developer and a city or county outlining the subsidies that the local government will provide to a project. Development agreements are intended to lock in certain development rights for a site with respect to what the developer can build so that the developer is not subject to the whims of future changes in elected officials who may not like the project as it was conceived and approved by previous officials. In exchange, the developer agrees to provide specified benefits and investments in infrastructure as part of the development. CBAs may be incorporated into development agreements.

Linkage and exactions

Linkages and exactions are popular mechanisms that local governments use to get new development projects to pay for affordable housing, parks, fire and safety, infrastructure, schools, hospitals, libraries, and other public benefits. Historically, new developments created additional needs for such services but did not pay for them. Beginning in the 1980s with impact fees, new development projects were charged with many such fees, sometimes to the point of placing heavy burdens on new homeowners.

While such fees are appropriate for making new development projects pay their fair share of the costs they impose on communities to provide these services, one of the downsides has been that municipalities shift an ever increasing share of these costs to new development. Impact fees totaling $60,000–$80,000 or more were not uncommon in California in the 2000s. Exorbitant impact fees raise the cost of new housing and apartments, placing an unfair burden on young homeowners and reducing housing affordability. Many communities in California, for example, were relying on development-generated fees to help pay for many services in the 1980s and 1990s and again in the 2000s. When severe recessions came in the early 1990s and in 2007–2009, the communities were strapped for cash and had to make severe cutbacks in services.

Linkages have become increasingly popular to help generate affordable housing. For example, developers may be required to provide 15 percent or 20 percent of new housing units that are affordable to people who make 80 percent of the median income in a city. Affordable housing may also be linked to commercial development. Sometimes the linkages fail to achieve the desired result. For example, downtown Los Angeles required major office developers in the 1990s to build off-site parking garages on the edge of downtown and were limited to how much parking they could build on-site in an effort to reduce downtown congestion. The
unintended consequence was that the new office buildings suffered for lack of on-site parking, and the new off-site parking garages went bankrupt when there was insufficient demand to cover their costs. Downtown Los Angeles became less competitive for tenants who preferred suburban locations where parking was accessible. The City of Los Angeles eventually did away with the requirement when the full effects became apparent—a costly lesson.

**Incentive zoning and value recapture**

Incentive zoning gives zoning bonuses in the form of higher FARs (Floor Area Ratios) for providing desired amenities. New York City, for example, gave developers up to 30 percent higher density for providing public open space such as plazas in front of their buildings. Mies Van Der Rohe’s Seagram building on Park Avenue pioneered the concept of setting the building back from the street with a large public plaza in front—a concept that changed the face of Manhattan.

Value recapture enables cities to generate ongoing revenues from new development. The Boston Redevelopment Agency (BRA), for example, gets 2 percent of the resale price for condos built on BRA land. The funds generated through the Value Recapture program help to provide a pool of money for affordable housing in other projects.

A related mechanism that institutions use to maintain affordable housing for university faculties and employees is through deed restrictions that require faculty to sell their homes to other faculty or to restrict the resale prices of the homes. Such programs enable universities, hospitals, and other institutions to maintain affordable housing for employees in high-cost areas such as Los Angeles and Cambridge. University Hill at the University of Irvine, California, for example, restricts the resale price of housing to the original purchase price plus the cost of improvements and certain fix-up expenses incurred for resale, adjusted by certain indices as described in the Ground Sublease. Furthermore, homes must be offered to faculty and staff in the university community, and owners may have to move if they no longer work for the university. The program has been very successful in maintaining affordable housing for faculty and staff in a high-priced area (Irvine Campus Housing Authority, 2016).

**Tax increment financing**

Tax increment financing (TIF) has become a favored mechanism for financing public contributions associated with new development. The boundaries of a TIF district are defined by the city or redevelopment agency to support bond financing of public facilities such as parking garages for a shopping area. The incremental property value increase associated with the new development is captured by the TIF district for purposes of generating taxes to pay interest and amortization on bonds which are sold to build the new garage. For example, suppose new development adds $600 million in property value within a TIF. If the tax rate is 2 percent, and 75 percent of the tax increment is captured by the TIF district, then $600 million \times 75\% \times 2\% = $8 million per year in taxes would be available to support the bonds. Municipal bonds are tax exempt (from federal income taxes) and carry lower interest rates than corporate bonds. If interest rates are, say, 4 percent, and the bonds have a 40-year term, then the additional taxes would support $158,340,000 in bond financing. Thus, the future incremental taxes can be used to support the sale of bonds which provide capital for constructing infrastructure and amenities to help improve the district.

TIFs are the most widely used local government program for financing economic development in the United States. However, the program has been the source of intergovernmental tension and
conflict over the using public aid for private benefit. Its popularity stems from a number of factors: It is highly decentralized. It reinforces the fiscalization of development policy. It plays off the fragmentation of local government and the competition among municipalities for investment and economic growth. And it fits well with the entrepreneurial spirit that characterizes contemporary local economic development policy (Briffault, 2010). Squires and Hutchison (2014) points out that there are downside risks with TIFs such as potential detriment to areas outside the TIF, local control over TIF spending, and what happens to TIF support for affordable housing when Redevelopment Agencies are abolished as they were in California in 2012.

Business Improvement Districts

Business Improvement Districts (BIDs) are another popular program for improving redevelopment areas, especially retail and business centers. BIDs were started to provide security, street lighting, benches, landscaping, and other amenities to improve the safety and desirability of shopping and business districts. The businesses within a specified geographic area agree to impose a special tax – usually 1 or 2 percent of property values – to support bonds for improvements similar to TIF districts and to provide funds for ongoing operations. The improved appearance and perceived safety of the district brings new customers and helps to raise retail sales and make the area more desirable for office tenants.

Summary

There are far too many topics relating to governance and land use policy relating to development to be covered in a single chapter. The present chapter has addressed a number of current programs and policies affecting development in the United States. Because most real estate and land use policies are implemented at the state and local level, different parts of the country are confronting different issues and are promulgating different programs and policies. In general, the coasts, and especially the gateway cities such as New York City, Los Angeles, Miami, Washington, DC, Seattle, and San Francisco are confronting problems of housing affordability and rising taxes associated with rapid urban growth. Those areas are more likely to have discretionary land use approvals by local city councils that raise the time, cost, and risk associated with obtaining entitlements for development. They tend to have more restrictive urban growth policies and a more aroused public who resist new development because of congestion, pollution, and other negative externalities from rapid growth. They are also more likely to have passed laws, such as California’s Proposition 13, that limit the ability of cities to raise property taxes. In a severely budget-constrained world, city officials are forever looking for new ways to raise money to pay for infrastructure and amenities to support growth. While the programs and mechanisms described in this chapter are hardly exhaustive, they provide insight into some of the recent trends and range of programs being adopted in different parts of the country.

Notes

1 Income property includes all investment property that generates lease income. It is typically held for several years. It is built using short-term construction financing, and when completed, is financed with a long-term permanent mortgage. For-sale property includes all real estate that is sold to end buyers (houses and condominiums) or to other developers (land). It is financed by short-term construction or land development loans.

2 \[ PV (4\% \text{ interest}, 40 \text{ years}, $8M \text{ payment}) = $158,340,000. \]
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