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Land Value Creation and Land Value Capture: Designing an Inclusionary Housing Ordinance Consistent with State Law

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Inclusionary Housing in Florida

In 2019, the Florida Legislature passed House Bill 7103, revising the legislative framework governing local governments' ability to adopt inclusionary housing ordinances (IHO). For the purpose of this report, IHO refers to all variants of local ordinances that ask developers of market-rate real estate development to build below-market-rate housing or make in-kind contributions. IHO used instead of Inclusionary Zoning (IZ), as many IHOs in practice are incorporated as part of the general ordinance, beyond the zoning section.

Most notably, HB 7103 added a new statutory mandate that requires local governments to "fully offset all cost" borne by the developers to comply with local IHO. The following subsections were added to the Florida Statute 125.01055, which applies to counties, and an identical set of stipulations were added to FS 166.04151, which applies to cities:

(2) An inclusionary housing ordinance may require a developer to provide a specified number or percentage of affordable housing units to be included in a development or allow a developer to contribute to a housing fund or other alternatives in lieu of building the affordable housing units. However, in exchange, a county must provide incentives to fully offset all costs to the developer of its affordable housing contribution. Such incentives may include, but are not limited to:

- (a) Allowing the developer density or intensity bonus incentives or more floor space than allowed under the current or proposed future land use designation or zoning;
 - (b) Reducing or waiving fees, such as impact fees or water and sewer charges; or
 - (c) Granting other incentives.
- (3) Subsection (2) does not apply in an area of critical state concern, as designated in s. 380.0552.

Confusion and misinterpretations followed the passage of HB 7103. Some local governments interpreted the amendment

as effectively prohibiting local governments' ability to adopt mandatory IHO. Others interpreted the new statutory mandate as writing checks to developers to reimburse the cost borne by the developers. In the least, HB 7103 has had a dampening effect on local governments' willingness to establish new IHOs. Sarasota County even repealed its existing IHO.¹

Value Capture and Inclusionary Housing Ordinances

"Value capture" refers to the idea that certain governmental actions increase the values of existing properties and new ground-up developments and thus, government entities should recoup some of this value increment for the public benefit (Calavita, 2015; Ingram & Hong, 2012; Kim, 2020). Applying this concept to IHO, governments can ask real estate developers to provide below-market-rate housing in return for offering a myriad of regulatory, administrative, and financial incentives that increase the profitability of proposed development projects. In fact, the revised legislative framework, which asks that incentives are provided to offset the costs, is firmly grounded on this concept of value capture.

There are three broad categories of government action that enhance the financial feasibilities of ground-up real estate developments. The first category is infrastructure investments, such as improvements to roadways, transit systems, and sidewalks. For example, if a new highway gets built through an undeveloped, rural area, the value of the raw land increases because of the enhanced accessibility to population centers. The second major category is land use and zoning amendments. For example, if local zoning is amended so that instead of only allowing for one unit per acre, twenty units are allowed, land will be valued at a much higher price because more housing units can be built on the site. The last category of action is other types of subsidies, which could be financial, regulatory, and administrative. An example of a common financial subsidy is property tax abatements. The valuation of commercial real estate works in a

¹ <https://www.heraldtribune.com/story/news/local/sarasota/2021/01/13/sarasota-county-guts-affordable-housing-requirements/4144609001/>

way that future discount on property taxes increase the present value of ground-up developments, which in turn increases the land value. Regulatory and administrative incentives, such as relaxing setback requirements and expediting the permitting process, could bring down the development and financing cost and thus, increase the profit margin for the developers.

component of IHO, the “value capture” step, can capture value by asking for developer contributions toward affordable housing. Table 1 below graphically illustrates the two distinct components of a well-designed IHO and lists some of the most common incentive options that local governments can offer.

Value Creation and Value Capture phases of Inclusionary Housing Ordinances

Value Creation (Incentives)	Value Capture (Below-market-rate housing)
<ul style="list-style-type: none"> • Upzoning (i.e., use, density, and height increases) <ul style="list-style-type: none"> ◆ Area rezoning ◆ Project-by-project negotiations ◆ Incentive zoning programs • Parking relief • Relaxation of design standards • Expedited permitting and building inspection process • Property tax abatements • Offering publicly-owned land at below-market price • Contributions to infrastructure (e.g., sidewalk improvements, utilities connection) • Fee waivers (e.g., building permit fees, inspection fees, etc.) 	<ul style="list-style-type: none"> • Build below-market-rate housing <ul style="list-style-type: none"> • On-site • Off-site • Alternative contributions <ul style="list-style-type: none"> • In-lieu fees • Land dedications • Conversion to affordable housing • Credit transfer

TABLE 1

Above actions, frequently undertaken by local governments, “create” significant value for real estate developers that can be used to “offset” the cost of providing below-market-rate housing, as mandated by the Florida Legislature. In Florida, specifically, agricultural lands are frequently turned into large scale developments and new towns enabled by amendments to comprehensive plans and local zoning ordinance. By simply increasing the allowable development density and intensity of rural and agricultural land, i.e., upzoning, rural communities of Florida have unlocked significant value for the developers of large-scale master planned communities (Ross & Outka, 2008). This added-value can be used to offset the costs the developers will bear as they comply with local IHOs.

Examples of IHO Design that Meet the Statutory Mandate

To successfully and safely satisfy the statutory mandate, we recommend conceptually distinguishing IHO into two distinct components (Kim, 2020). The first component of IHO should offer incentives, such as allowing for greater density, which could be classified as the “value creation” step. Subsequently, the second

The two-tier approach to IHO can be crafted in several different ways (Table 2). An IHO can encompass both the value creation and capture components, or it can be designed to include the value capture component only but triggered when value creation takes place. An example of the former is Denver’s IHO that requires developers to set aside 10% units as affordable and in return offer a menu of cost offsets, which could be a combination of density bonus, up to \$25,000 reimbursement subsidy per unit for up to 50% of new units, parking requirement reductions, and expedited permits. An example of a latter is Boston’s IHO that requires developers to set aside 13% units as affordable, but only triggered when developers seek any type of zoning relief or when projects are financed or subsidized by the city. Another variant of the latter approach is Seattle’s IHO, where the city adopted a citywide rezoning that increased the allowed density and intensity of development citywide and created a mandate to set aside below-market rate units in return. These examples are grossly simplified for illustrative purposes. The actual ordinances are highly complex and varied in their application.

These different courses of actions for crafting IHOs may be combined to create a multi-pronged approach. For example, a city/county might have a city/countywide IHO that is only triggered when certain thresholds are met (e.g., when new planned unit development is established), while also establishing area-specific incentive zoning programs where

developers can opt to take advantage of additional incentives in exchange for making a greater contribution towards below-market-rate housing. Calavita and Mallach (2009) argue that the rezoning approach, such as that of Seattle's, is the best option as it ensures that the cost of providing below-market-rate housing gets passed on to the landowners, not to future renters and homebuyers or the general public.

Design alternatives for the two-step Inclusionary Housing Ordinances

Design Option #1	Design Option #2	Design Option #3
		
<p>Example: Denver, CO</p>	<p>Example: Boston, MA</p>	<p>Example: Seattle, WA</p>
<ul style="list-style-type: none"> • Requires developers to set aside 10% units as affordable and in return offer a menu of cost offsets • A combination of density bonus, up to \$25,000 reimbursement subsidy per unit for up to 50% of new units, parking requirement reductions, and expedited permits 	<ul style="list-style-type: none"> • Requires developers to set aside 13% units as affordable • Only triggered when: <ul style="list-style-type: none"> ◆ developers seek any type of zoning relief ◆ when projects are financed or subsidized by the city 	<ul style="list-style-type: none"> • Adopted a citywide rezoning that increased the allowable density and intensity of development across the board • Created citywide IHO that mandates developers to set aside below-market rate units

TABLE 2



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