



LAND VALUE RECAPTURE TO FINANCE INFRASTRUCTURE

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LAND VALUE CAPTURE (LVC) UNDER CONNECTICUT LAW

Connecticut law allows local government entities to use certain LVC methods to finance new infrastructure. These methods generate revenue by "capturing" the increase in the value of property located near the new infrastructure.

Water pollution control authorities and special taxing districts often finance new infrastructure by levying "benefit assessments" on those properties that especially benefit from the infrastructure.

Municipal redevelopment agencies may finance infrastructure and other public improvements in a designated redevelopment area by capturing the increase in the property tax revenue those areas generate (tax increment financing). The increase results from the increase in property values the new infrastructure triggers, not from a special tax or assessment.

ISSUE

Explain "land value capture" (LVC) in the context of transportation infrastructure financing.

SUMMARY

LVC is a way to finance certain types of public infrastructure by capturing some of the additional value it creates for adjacent property. For example, a landlord may be able to charge higher rents for an apartment near a subway stop because people who want to get to work quickly are willing to pay more for this benefit. Likewise, those who operate a business near the stop potentially benefit from the flow of people approaching or leaving the station. Those benefits take the form of increased property values and, with respect to businesses, profits.

LVC methods convert the incremental value generated by the infrastructure into contributions, taxes, or fees that supplement the revenue generated from traditional sources, such as fares, tolls, and property taxes. For example, the fares commuters pay for rail service help cover the rail line's operating cost and debt service. The general taxes commuters, other members of public, and businesses pay also go toward paying these costs.

But taxes, fees, and other traditional sources no longer seem to generate enough revenue to build and operate infrastructure at affordable costs. Fareboxes for many of the world's most famous public transportation systems do not generate enough revenue to cover operating costs and other expenses, stated Deborah Salon, a researcher at the University of California, Davis, " Institute of Transportation Studies. Consequently, "substantial government subsidies are required to build, maintain, and operate most public transport systems," she added. ([Location Value Capture Opportunities for Public Transport Finance](#), May 2014).

Some LVC methods attempt to close this revenue gap by seeking payments from benefiting property owners or leveraging private investments from businesses that propose to develop and operate the infrastructure under a public-private partnership agreement (development-based methods). Other methods impose taxes and fees on the property that most benefits from the infrastructure (tax-based methods).

LVC methods face different challenges. Public-private partnerships are relatively new concepts, and many public agencies lack the knowledge, skill, and experience to negotiate them. (OLR report [2014-R-0010](#) provides background on these partnerships.) Tax-based approaches work best if the (1) tax generates a consistent and steady revenue flow and (2) method effectively isolates the value the proximity to the infrastructure contributes from that contributed by broader economic factors, such as a building boom. The tax also must not burden some taxpayers more than others, such as elderly people on fixed incomes who own valuable property.

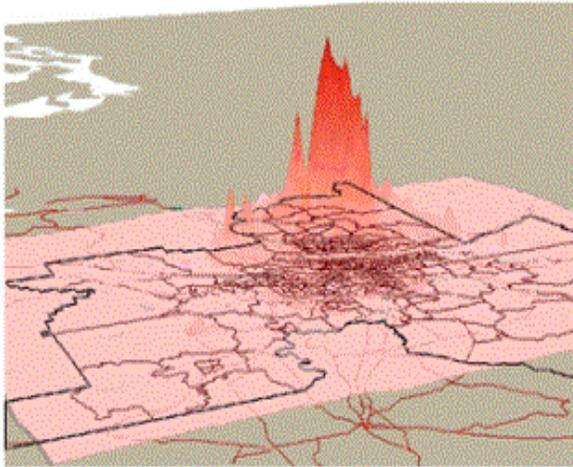
VALUE TO BE CAPTURED

LVC methods help finance public improvements by capturing some of the value that typically accrues to property located near such improvements. For example, the closer a store is located to a new subway stop, the easier it is for its customers to get there. The stop's location makes it convenient for people who live, work, or shop in the immediate area, thereby making the area desirable to other people and organizations. That desire could increase the demand for property in the area and consequently drive up real estate values. Policy analysts refer to this increase in value as the "unearned increment" to distinguish it from the incremental value property owners and tenants create when they improve their property.

Graphic 1 shows how the concentration of public infrastructure and other amenities in city centers increase land values. The actual incremental value they create depends on several factors. For transit systems, those factors include the service

Graphic 1

Portland Oregon LandValueScape



Source: <http://www.earthrights.net/images/mod5-038.gif>

being provided (bus, rail, or highway), the service's quality, other available means of transportation, a property's distance from the system, and a property's use (apartment, store, or offices).

However, other factors could make it difficult to isolate the unearned increment the system creates for surrounding property. For example, zoning changes could

drive up land values by allowing previously prohibited land uses, and economic development tax incentives could attract new development.

LVC METHODS

LVC methods capture value differently. In a [paper](#) written for Ontario's transportation agency (Metrolinx), the George Hazel Consultancy divided them into two broad categories.

Development-based methods obtain (a) private capital from businesses that agree to develop and operate the infrastructure under a partnership agreement with a government agency or (b) contributions from the owners of private property that especially benefit from the infrastructure.

Tax-based methods require these owners to pay a special tax or fee that is used to repay bonds issued to finance the infrastructure. In practice, most LVC methods are hybrid, mixing development- and tax-based methods, "depending on local circumstances and the development patterns and potential," the report states.

Development-Based Methods

Development-based methods are potentially able to raise more revenue than tax-based ones, the report states, because the contributions go only toward the infrastructure that creates the incremental value. In some public-private partnerships, private developers invest their own capital to develop the infrastructure in return for the right to operate it.

Some development-based methods finance new infrastructure with contributions from property owners who especially benefit from the infrastructure. In these cases, the report advises government agencies to reach an agreement on the contributions before the construction begins to mitigate land speculation. "The largest gains are to be made in the initial stages of the development process before options are taken and site ownership transferred...As time goes by, and certainty increases, value is taken out as developers anticipate increases in land value around the new transit."

Development-based approaches work best with proposed transit stations and other fixed transit infrastructure when the owners of the benefiting property believe government does not have enough revenue to start the work. "If landowners and developers think that the new transit facility will be 100% funded by the public sector there will be reluctance to contribute to the funding through LVC gains," the report stated. Lastly, development-based methods work when the interests of all the stakeholders align.

Unlike the tax-based approaches discussed below, development-based approaches do not pose significant efficiency or equity issues, according to the report. Because they involve the sale or lease of infrastructure or development rights, public agencies and private developers can address them as they negotiate the sale or lease agreement. But, as Salon stated, "these strategies can be somewhat risky for the public agency if that agency does not have the internal capacity to properly negotiate a good contract." For example, she states the New York Metropolitan Transportation Authority's development rights contract for the Atlantic and Hudson rail yards was recently criticized as being too favorable to developers.

Tax-Based Methods

Tax-based methods capture the incremental value resulting from new public infrastructure by taxing some of that value. Table 1 summarizes how these methods work.

Table 1: Tax-Based Approaches

<i>Method</i>	<i>Description</i>	<i>Taxpayer</i>	<i>Timing</i>	<i>Geographic Jurisdiction</i>
Special Assessments	Fee imposed on property directly benefiting from new infrastructure (e.g., stores adjacent to a commuter rail stop)	Owners or tenants of property especially benefiting from the infrastructure	Ongoing	Designated district
Tax Increment Financing	Increase in property tax revenue generated in designated redevelopment areas	Property owners	Ongoing	Designated district
Development Impact Fees	Fees imposed on new private development	Developers	One-time	Limited to new private development near the infrastructure

Source: Salon, *Location Value Capture Opportunities for Urban Public Transport Finance* (2014)

Salon identified several issues with tax-based approaches, as noted below.

Revenue Volatility. Because these methods attempt to capture value through a specific tax, they are vulnerable to economic trends that affect the tax’s revenue flows (volatility). For example, “value capture mechanisms that are tied to specific real estate markets can fluctuate with the rhythms of those markets” while those tied to new development (impact fees) “will yield revenue streams that rise and fall with booms in construction.”

Government agencies can compensate for this volatility in boom years by depositing surplus revenue in rainy day funds. But “most public agencies do not have experience with managing such volatile revenue streams, and this is difficult to do well because it is not clear whether the current situation is part of a cycle or part of a trend,” Salon stated.

Efficiency. A LVC method is efficient when it captures only the incremental value attributed to the new infrastructure, but value cannot always be isolated from other sources that increase property values, such as museums, parks, and other local amenities. LVC mechanisms that capture value generated by these and other sources put “negative pressure on local economic growth.” Methods that impose fees on new development, for example, may increase construction costs or possibly discourage new construction.

Equity. Salon identified several equity issues associated with tax-based methods. Capturing the value accruing to residential property could impose a financial burden on property owners on limited incomes, such as senior citizens. Capturing the increase in property tax revenue from a designated area to finance new infrastructure is equitable if that infrastructure created the value. It is less equitable if value was caused by other factors, such as a citywide building boom. In these cases, the area's property owners actually "contribute less to the overall city budget than they would otherwise," thus creating "an equity imbalance between those in the zone and those outside it."

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