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HARNESSING LAND VALUE CAPTURE

Municipal Public-Private Partnership

Framework

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Purpose of the Module

This module introduces concepts of land value capture and describes a few of the key instruments that municipalities can use to capture land value.[1]

[1] For a more complete discussion of this topic, see Amirtahmasebi, Rana, Mariana Orloff, Sameh Wahba, and Andrew Altman. *Regenerating Urban Land: A Practitioner's Guide to Leveraging Private Investment*. 2016. Urban Development Series. Washington, DC: World Bank. doi: 10.1596/978-1-4648-0473-1; Smolka, Martim O. 2013. *Implementing Value Capture in Latin America: Policies and Tools for Urban Development*. Lincoln Institute of Land Policy.

2.0
The Importance of Land for Municipalities

Land is the most valuable asset for municipal governments. The sale or lease of land may represent a significant potential revenue stream for the municipality. The city government of Istanbul, Turkey, auctioned and sold an old municipal bus station and administrative building in 2007 for US$1.5 billion. Comparing this with its total municipal capital spending of US$994 million, one can see the potential of land as an asset. Similarly, in Mumbai, India, the city earned US$1.2 billion from the sale of 13 ha of land in the city's new financial center, totaling 10 times the city's capital spending in 2005. But, land is a limited and non-renewable asset and urban land markets are extremely volatile.[2]

[2] For a more complete discussion of this topic, see Amirtahmasebi et al. 2016;. Smolka et al. 2013.

3.0 Understanding Land Value Capture

The notion of 'land value capture,' is to mobilize some or all of the land value increases resulting from actions other than the landowner's, such as public investments in infrastructure or administrative changes in land use norms and regulations, for the benefit of the community at large.[3] Thus, the objective of land value capture is to draw on publicly generated land value increases to enable local administrations to improve their land use management practices, and to help them fund more urban infrastructure and service provision. A simple example is property tax, which requires landowners to share a percentage of land value with the municipality. The amount of property tax paid increases as the value of the land increases (no matter the cause of the increased value).

In practice, successful implementation of land value capture demands management skills to deal with many complex factors and diverse stakeholders. In addition, it requires proper understanding of land market conditions; comprehensive property monitoring systems; a fluid dialogue among fiscal, planning, and judicial entities; and the political resolve of local government leaders.[4] Land value increases are captured more successfully from landowners and other stakeholders who perceive they are receiving greater benefits from a public intervention than those accruing from business as usual and are more likely to succeed when used to solve a locally recognized problem.[5]

[3] For example, the principle may exist at law that no citizen should accumulate wealth that does not result from his or her own efforts, known as 'unjust enrichment' in both civil and common law traditions. Smolka et al. 2013.
[4] Smolka et al. 2013.
[5] Smolka et al. 2013.

4.0 Instruments for Land Value Capture

Key instruments available to a municipality to implement land value capture include the following:[6]

(1) **Land as public contribution** - when a municipality uses the value of its land as an equity contribution toward a PPP. In this scenario, a public entity might enter into a partnership with a PSP for redeveloping a targeted urban area. The public sector 'invests' the value of its land assets and the PSP invests cash.

(2) **Developer exactions and impact fees** - the developer is required to contribute to public services as a precondition to developing a plot of land, as compensation for the cost of additional public infrastructure and services. For example, developer exactions may include the following:
- Dedication of land for public use, for example, reserving a certain percentage of land for parks, public space.
- Construction of public improvements, for example, the developer constructs a public road to connect the proposed development with the existing public road network.
- Funding, for example, the developer provides a financial contribution toward the cost of a new bus stop or LRT station

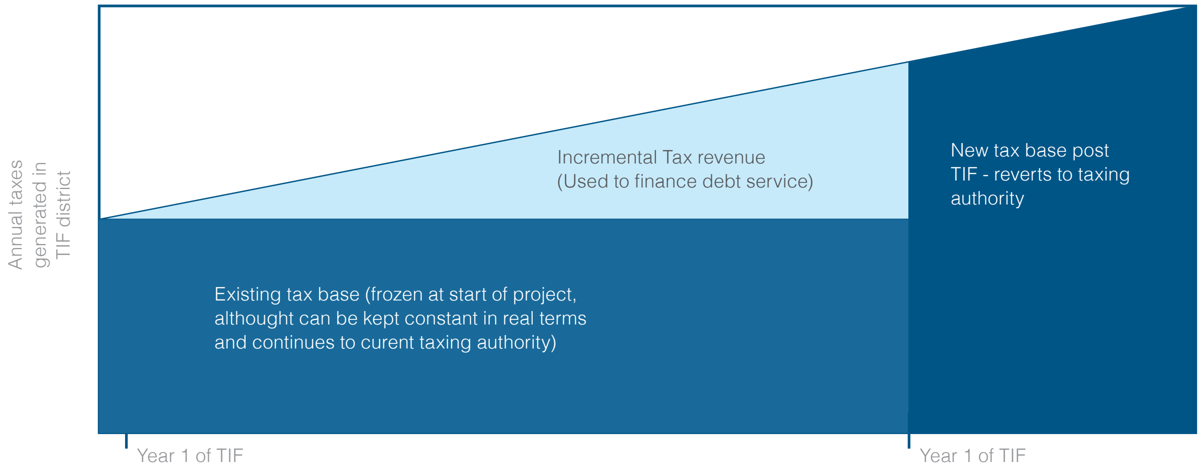
Among the disadvantages of this financing tool is that it can be technically cumbersome to estimate appropriate costs. Any government discretion regarding assessment amounts can create perceptions of corruption. Also, with the exception of some robust real estate markets (for example, Hong Kong, SAR, China), imposing an extra levy can at times have the effect of discouraging, rather than incentivizing, private sector investment.

(3) **Betterment levies** - a form of tax or a fee levied on land that has gained in value because of public infrastructure investments. For example, in Johannesburg, South Africa, city improvement districts (CIDs) are defined geographic areas in which property owners agree to pay for supplementary services and improvements in their urban environment. These services can include security measures, urban area upgrades, litter collection, and design and upkeep of public spaces. A CID can be formed when a petition is filed by at least 51 percent of the property owners in the geographic area and then approved by the municipality. The CID levy is compulsory and is calculated based on the value of the individual property and applied pro rata. While it is considered one of the most direct forms of value capture, the cost of administering parcel-by-parcel betterment levies can be high compared to the collected revenue.

(4) **Tax increment financing (TIF)** - the municipality issues a bond on the capital markets to borrow against forthcoming increases in tax receipts that accompany successful urban redevelopment. The tax revenues yielded, which exceed the taxes that would have been collected without the redevelopment, constitute the 'tax increment' and the TIF captures that gain to pay the bond holders. A TIF allows the municipality to invest in public infrastructure and other improvements by borrowing against the future anticipated increase in tax revenues generated by the project. A TIF can facilitate the self-financing of a project with minimal negative fiscal impact. This tool is less appropriate for less developed financial markets or for funding smaller projects.

[6] Amirtahmasebi et al. 2016.

Figure 1. The Basic TIF Model



(5) **Density bonus** - a municipality may permit a developer to increase the maximum allowable development on a site in exchange for either funds or in-kind support. For example, the municipality may allow landowners near the new infrastructure to increase the type of development allowed, permitting the developer to earn more from the land. In exchange, the landowner must pay a fee for the development rights. This fee is used to fund infrastructure. This tool works best in cities in which market demand is strong and land availability is limited, or for projects or sites in which the developer's financial incentives outweigh alternative development options.

(6) **Up-zoning** - changing the zoning to allow for higher value (for example, from industrial to residential) or more dense use (for example, increasing allowable floor area ratio). As with density bonuses, up-zoning can be successfully deployed as a kind of financing tool for urban regeneration only when sufficient market demand exists.

5.0
List of References

Amirtahmasebi, Rana, Mariana Orloff, Sameh Wahba, and Andrew Altman. *Regenerating Urban Land: A Practitioner's Guide to Leveraging Private Investment.* 2016. Urban Development Series. Washington, DC: World Bank. doi: 10.1596/978-1-4648-0473-1

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