

What is the effect of value capture districts as they relate to financing transportation services?

There is fierce competition at all levels of government for access to the limited pool of resources available to fund capital improvements. An aging and overburdened transportation infrastructure is demanding an increasing share of available funds at the same time traditional funding sources (i.e. the federal government) are drying up. The inability of traditional funding sources to meet the demand for infrastructure improvements has forced transportation planners and policy makers to search for alternative sources of funding. (Walther et al., 1991)

Value Capture is one alternative funding source option. Value capture refers to a type of public/private partnership in which the private sector compensates a public agency for the cost of a facility that generates economic value (Hyman, 1997). Transportation projects, including interchanges, new freeways, and public transit stations, can create or improve the adjacent market for new development, and thus generate a windfall for private landowners. The goal of a value capture program is to 're-capture' for the public good some of the unearned economic benefits realized by the private sector owners. Land value is the most common measure of realized benefit. (Walther et al., 1991) While value capture is primarily an infrastructure finance tool, policy makers and planners are in a position to use these development techniques to induce more 'positive' forms of growth and to ameliorate externalities imposed on the public under previous funding programs. (Batt, 2001).

Fundamental Principles

Two fundamental concepts, *Public Purpose* and the *Origin of Land Values* serve as the foundation for value capture policies.

Public Purpose – As with any public policy or program, there needs to be a strong rationale made for any government involvement at all. Public finance has traditionally recognized three broad justifications for public intervention: economic stabilization, income re-distribution, and efficient resource allocation. (Abouchar, 1977) The allocation of public resources is typically reserved for correcting market failures, like the under-production of public goods, and externalities. In some cases, especially related to transportation infrastructure and land assemblage, the legal and administrative efficiency of involving governmental authorities justifies public involvement.

While public purpose is a precursor for projects involving the use of eminent-domain, value capture techniques in general are held to be legal and legitimate when (1) the public infrastructure improvement is required to accommodate growth, (2) the revenue generated does not exceed the actual costs of the improvement, and (3) the revenues are only spent for the purpose for which they were raised. (Walther et al., 1991)

Origin of Land Values – Land value, according to Batt is, “a function of the social and economic traffic that the land generates. Excluding resources that a parcel of land may contain (lumber, minerals, water etc.) it has economic value solely by virtue of its location. It is not what any lone individual does that makes a parcel of land valuable; rather it is through joint community effort that land acquires worth.” (Batt, 2001)

When the public makes an investment in infrastructure, increasing for example access to a particular parcel of land, the value of that land increases through no effort by the owner. Any value change experienced by the landowners in proximity to the publicly funded infrastructure is therefore “unearned”. The value of the unearned benefit should, according to the theory, accrue to the public agency that incurred the cost of constructing the public facility that increased the value of the private land. (Callies, 1974)

The ability to recapture unearned gains has appeal from both a public relations and public policy perspective. According to Daniels, “economists almost universally agree that unearned increments or economic rents to bare land can be taxed away without any disruption to economic efficiency or diminution of the value or income of land improvements.” (Daniels, 2001) Batt makes a similar claim when he states, “Using a tax on land values that benefit from particular capital investments satisfies all the virtues of sound taxation theory. Unlike finance methods that rely directly or indirectly on income, sales, or franchise taxes, a levy on land correlates well with benefits received, and is likely to be stable, simple, administrable, progressive, and most of all efficient. It is efficient, because it is economically neutral.”

Methods & Techniques

Value capture is not a single financing tool, but rather a toolbox of financing techniques. These tools, however, generally fall into one of three categories. (Callies, 1979)

Development of Air Rights – The development of new transportation infrastructure often results in large amounts of land reserves for right-of-ways.

The sale of the development rights over tracks, highways, stations etc. is a common way of recapturing construction costs.

Excess Condemnation & Disposal – If the purpose of the land acquisition is not solely to recapture the cost of the public expenditure, public agencies can often condemn more land than is directly required for the project. The sale of this excess property once the land value increases have been realized can be used to recapturing construction costs. Agencies using this method must be careful to avoid claims of a ‘taking’. Courts have generally allowed ‘excess condemnation’ in cases where the additional land was [1] essential to the business success of the new operation (e.g. for a transit development a parking lot and small retail area could be claimed as essential for the success of the station.), [2] required for a future use or expansion, [3] necessary to protect the value of the investment, or [4] prevent the creation of valueless parcels.

Monetary Transfers – This category of value capture techniques encompasses a much larger number of tools than either of the previous two categories. Some of the more common techniques include:

- Special Benefit Assessment – Projects are often considered to create a special benefit to particular property owners over and above the general benefit enjoyed by the broader public. Special assessments and taxes are imposed on landowners within a reasonable distance of the improvement. Land value based taxes are generally considered to be progressive as the levy corresponds well with the benefits received. (Batt, 2001)

- Impact Fees – Various forms of impact requirements are the most frequently used of the monetary transfer techniques. To prevent an abuse of powers by the government, to impose an impact fees the authority must be able to show a reasonable relationship between the requirement and the costs incurred and that the development paying the fee obtains a benefit from its payment. Impact fees are most effective in areas experiencing strong growth. Impact fees are also from an equity standpoint considered a regressive form of taxation as levels are set not by ability to pay but by actual costs incurred.(Walther et al, 1991)
- Tax Increment Finance (TIF) – TIF programs capture the net increase in property tax revenues resulting from development in a defined district for use in funding the ‘public’ portion of the developments capital cost. TIF is a widely used development tool in 44 states. In most states TIF can only be used in cases where ‘but-for’ the captured value no development would occur. Arguments are often made the TIF is an inefficient economic subsidy that results in over-investment in low-growth areas and under-investment in high growth areas. (Dye, 2000)

Conclusion: The Reality of Value Capture Policies

“As local and state governmental units providing the public sector enhancement frequently lack the up front funds to make the improvement, value capture, in practice, becomes ‘enhanced value anticipation capture’ where the public sector claims a share of the anticipated increases in private sector value prior to the implementation of the public sector improvement.” (Walther et al., 1991)

This statement, taken from a report prepared for the US Department of Transportation, provides an excellent summary of how value capture is applied in real-world situations. Value capture is difficult to apply proactively. In the best of circumstances, public agencies are required to provide some form of bridge financing between the time when the project is completed and when the unearned value is captured. While a number of administrative and logistical issues (where to draw district boundaries, how to assess ‘unearned’ gain and future land value) must be addressed to make value capture work these issues are not insurmountable.

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