Chapter 4

Government Controls and Real Estate Markets

Features of Real Estate that Cause Market Distortions

• “Spillover” effects from nearby land uses
• Uniqueness of location (absolute monopoly)
• Instability of surrounding land use
• Unknown quality or condition of existing structures

Resulting Market Failures in Real Estate

• Monopoly
  – Utilities
  – “Holdouts” in land assembly efforts (roads, other public uses)
• Externalities
  – “Spillover” effects of land use for which initiator is not held accountable (traffic congestion; runoff; smoke, gases, and particle emissions; noise; urban sprawl; disorderly extension of urban infrastructure)

More Market Failures (continued)

• Incomplete information
  – Construction quality hidden
  – Buyers unaware of structural risks of hurricanes, etc. (maximum wind tolerance of structure; safety of electrical or gas systems; fire dangers)
• Uncertainty of residential values
  – Effect (“weird” structures; nonresidential land uses; students)

The “Revolution” in Land Use Controls

• Pre-1970: Little interest in land use controls
  – No plans had force of law
  – Zoning very limited in function
    • Focused on protection of single-family homes
    • Did not exist in many areas
• Environmental movement of late 1960s
  – Rachel Carson: Silent Spring
  – Love Canal
  – Notion of “spaceship earth”
Comprehensive Planning as a Solution to Market Failure

- Project future population growth
- Determine requirements for water and waste disposal
- Project needs for public services (utilities, streets, schools, parks and recreation, safety)
- Projected demand for various land uses (public, residential, nonresidential)
- Design compatible arrangement of needed land uses (land use map)

Urban Planning is Needed for Storm Water Management

Urban Planning is Needed for Traffic Management

Urban Planning is Needed for Schools and other Services

Challenges to Public Land Use Planning

- Changing notion of “best practice”
  - Cul-de-sacs or grid streets?
  - Mixed density and use or containment of nonresidential use?
- Limited actual experience to rely on (less than 30 years)
- Insufficient theory and information
- Inability to foresee the future well

Traditional Planning vs. New Urban Planning

Traditional
- Separated uses
- Automobile oriented
  - Priority placed on easy ingress and egress
- Uniform density
- Cul-de-sac hierarchy in neighborhoods
Traditional vs. New Urban

Denver Style – Away from New Urban

Traditional Land Use Controls:
- Building Codes
  - Older than zoning (circa 1900)
  - Issues of safety
    - Fire: Materials, alarms, electrical and gas systems
    - Sanitation: Plumbing, water, and HVAC requirements
    - Injury: Design and strength
  - Continue to evolve
    - Effect of Hurricane Andrew, 2004-5 hurricanes, Katrina
    - New technology (e.g., smoke detectors)
    - Changing perception of needs (e.g., bedroom windows large enough to step through)

Traditional Land Use Controls: Zoning
- Features of traditional zoning
  - Use classifications: Residential, commercial, industrial, automotive
  - Use districts (zoning map)
  - Setback requirements
  - “Bulk” or density limits (minimum lot size, height limits, maximum floor area ratios)
  - Special use districts: Service stations, hospitals, churches, private schools, cemeteries

Building Codes Establish Minimum Requirements

Carl Siebert, South Florida Sun Sentinel
Traditional Land Use Controls: Subdivision Regulations

- Features of subdivision regulations
  - Standards for streets, sewers, and water systems
  - Adequate water supply for fire safety
  - Adequate drainage and run-off retention
  - Open spaces
  - Lot layout
  - Easements for utilities
  - Traffic and pedestrian safety

Traditional Land Use Controls: Planning and Zoning Administration

- Planning and Zoning Commission created in ordinances
- Requested changes must:
  - Be compatible with a comprehensive plan
  - Be justified if they require change in the comprehensive plan
  - Not have undue effect on surrounding land uses or the community
- Commission ultimately serves as advisory to elected officials

Traditional Land Use Controls: Board of Adjustment

- Reviews petitions for variances
- Decisions are final rather than advisory to the elected officials
- Only appeal is through the courts

Traditional Land Use Controls: Site Plan Review

Zoning Issues and Concepts

- Legality of zoning: Village of Euclid vs. Ambler Realty - 1926
- Nonconforming use: Use inconsistent with and precedent to zoning map
  - Cannot be substantially changed
  - Must be continuous
  - Can be “amortized” away, (e.g. billboards)

Zoning Issues and Concepts (continued)

- Variance: Exception to requirements due to hardship
- Exclusionary zoning (unreasonable lot size; inadequate provision for low- and moderate-income housing)
Do Land Use Controls Solve the Problem of Market Failure?

- Does zoning raise the cost of “threshold” housing unnecessarily?
- Do land use controls interfere with economically efficient land use patterns? (Example: Does zoning make neighborhood services excessively remote)
- Does low density resulting from zoning contribute to urban sprawl?
- Houston: effective land uses without zoning?

Newer Approaches to Land Use Control

- Planned Unit Development
  - Mixed density
  - No setback requirements
  - Open community spaces
  - Community facilities
  - Mixed uses
  - Negotiated “contract” with land use authorities

- Performance standards
  - Runoff limits
  - Noise and emission limits
  - Traffic limits
  - Tree removal restrictions

More New Land Use Controls

- Impact fees
  - Favorite of economists (in principle)
  - Despised by many in the building community
- Growth restrictions
  - Temporary moratoriums
  - US Supreme Court refuses to review Petaluma, Ca. limit on the number of new housing units.
  - Also Boulder, Co. and Boca Raton, Fl.

Power of Eminent Domain

- Eminent domain: Right of government to acquire private land, without the owner’s consent, for public use, with due process and just compensation
- Condemnation: Legal procedure for exercising the right of eminent domain
  - Public use vs. public purpose
  - Just compensation based on highest and best use
  - Problems of excessive use
- Inverse condemnation

Eminent Domain Controversy - I

- Concept of “public use” expanded to “public purpose”
  - US Supreme Court in 1954 allowed condemnation of “blighted areas” for private redevelopment
  - Michigan Supreme Court in 1983 allowed condemnation to enable GM manufacturing facilities
- Wide-spread subsequent condemnation of “blighted areas” for private redevelopment
- Driven by local government hunger for an increased property tax base

Eminent Domain Controversy - II

- Kelo v. New London Ct., 2005
  - U. S. Supreme Court allowed use of eminent domain to obtain non-blighted property for private redevelopment
  - Left it to states to decide whether to intervene
- Most states initiated legislation to limit use of eminent domain
- Congress enacted law to prevent application of Federal monies for such use
- Most states dropped the proposed laws to limit eminent domain
Sample of Environmental Controls since the Late 1960s

- Clean Air Act
- Clean Water Act
- Comprehensive Environmental Response Compensation and Liability Act (CERCLA)
- Occupational Safety and Health Act (OSHA)
- Endangered Species Act

Hazardous Materials Issues

- Asbestos and fiberglass
- Polychlorinated biphenyls (PCBs)
- Leaking underground storage tanks (LUSTs)
- Lead paint
- Radon
- Mold

Environmental Assessments

- Phase I EVA (noninvasive)
  - Air and water samples
  - Historical property records
  - Site inspection
- Phase II EVA
  - More invasive tests to confirm indications from Phase I
- Phase III EVA
  - Complete assessment of extent of the problem
  - Determination of remediation needs
  - Estimation of remediation cost
  - Prescriptions for future prevention

Property Taxes

- Primary source of local government revenue
- Reliable and countercyclical
- Many taxing authorities
  - City
  - County
  - Transportation authorities
  - Schools
  - Water management districts
- Property Tax Exemptions
  - Religious organizations
  - Nonprofit organizations
  - Homestead
  - Educational institutions

Determination of Tax Rate

\[
\text{Tax rate} = \frac{\text{Total budget of Taxing Authority} - \text{Income from other sources}}{\text{Total assessed value} - \text{Total value of property exemptions}}
\]

\[
R_T = \frac{(E_a - I_o)}{(V_f - V_e)}
\]

\[
R_T = \frac{(65,000,000 - 25,000,000)}{(2,500,000,000 - 500,000,000)} = .020
\]

Or, a tax rate of 2 percent.

Or 20 mills

Computing Tax Liability

- Market value: $150,000
- Assessed value: $135,000 = (0.90 \times MV)
- Less: exemptions: $25,000
- Taxable value: $110,000

Property Tax Calculation

- County: 8.58 \times $135,000 = $1,160.70
- City: 3.20 \times $135,000 = $432.00
- School district: 9.86 \times $135,000 = $1,338.60
- Water mgt. district: 0.05 \times $135,000 = $67.50
- Total: $2,160.80

Taxes Levied: $2,385.90
Special Assessments

• Special assessments: Taxes for specific public improvements affecting a property
  — Street, sewer, etc.
  — Usually charged on a per front foot basis
• Example: Street improvements of $500 per running foot of street
  — For lot with 100 feet of frontage:
    \[100 \times 0.5 \times 500 = 25,000\]

Issues with Property Tax

• Regressive
• Uneven across geographic areas
• Poorly administered

Special Assessments and Community Development Districts

• Many large subdivisions have private community development districts
  — Create and maintain neighborhood infrastructure
    • Utilities
    • Drainage and water retention
    • Streets, bikeways, walkways
    • Recreation facilities
• Issue tax-exempt bonds and impose property assessments to pay the obligations
• Have the same lien priority as property taxes

End of Chapter 4