THE MINNEAPOLIS 2040 PLAN IS UNLIKELY TO PROVIDE AFFORDABLE HOUSING

BY MATT LEICHTER

On October 25, 2019, the Minneapolis City Council approved the "Minneapolis 2040" plan. City officials produced it to guide the development of Minnesota's largest city into the mid-21st century. The plan focuses on a variety of developmental areas, such as jobs, education, the environment, and transportation.

The plan's objectives for each of these areas didn't raise much controversy, except in one: housing.

The controversy arose because the Minneapolis 2040 plan does something that no other major American city has ever attempted: it shifts zoning practice away from real-estate parcels for single-family use. No, it doesn't abolish them altogether, thus forcing homeowners to build condos or apartment buildings. Rather, the plan permits homeowners in the least developed parts of Minneapolis to upgrade their lots into duplexes or triplexes. Landowners living along transit corridors will have even greater development options. This policy, referred to as "upzoning," is popular among urban advocates, and until now cities have only implemented it piecemeal. The plan's purpose for these ambitious changes includes increasing the availability of affordable housing, reducing rents, and helping realize the mayor's goal of racial justice.

Unsurprisingly, then, the plan's opponents alleged it would destroy their neighborhoods, while housing advocates, pleased the plan passed at all, lamented that the option of building quadraplexes on single-house lots had been negotiated away. With so much at stake, it's worth asking whether the plan will increase the housing supply as the advocates hope, or will this attempt to create affordable housing falter as others have?

The short answer is, as I predict: it will falter.

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Now for the long answer. First of all, let's be clear: The Minneapolis 2040 plan doesn't require anyone to do anything any time soon. It doesn't change incentives as rapidly as a tax could. We know this because according to Minnesota Public Radio, there aren't many projects pending the City Council's final approval of the plan. (cont'd on pg. 6)

FEATURED PROJECTS

RSF CONDUCTS AND SUPPORTS WORK IN COMMUNITIES, EDUCATION, OUTREACH, AND PUBLISHING

NATIONAL TAX ASSOCIATION CONFERENCE SPONSORSHIP

TAMPA, FLORIDA
NOVEMBER 20-23

The National Tax Association (NTA) is a nonpartisan and nonpolitical educational association, which does not promote any particular tax agenda. Instead, it is "dedicated to "advancing the theory and practice of public finance, including public taxing, spending and borrowing," and counts among its membership, government officials, corporate representatives, and academic and independent researchers.

Recognizing the intersection of missions and opportunity to learn about research in taxation, RSF sponsored the NTA's annual conference and Josie Faass and Brendan Hennigan attended the event, where they heard numerous presentations on property tax assessment and administration.

The NTA sponsors. Can you spot RSF's logo?

STUDENT INTERNSHIPS

WITH RSF AND CPTR

Research and education represent core focal areas of RSF's new strategic plan, so it's only natural that we should seek to foster new partnerships with academic institutions. Add to this the fact that the newly formed Center for Property Tax Reform (CPTR), has an emphasis on outreach and the provision of data to support community-specific tax reforms, and the perfect opportunity to engage student interns in support of the production of real world analyses and research results.

RSF and CPTR are currently in conversation with several Pennsylvania and New Jersey universities, and expect to hire 1-2 graduate student interns to support our efforts!

Impacts of Land Taxes in Thailand
(cont'd from pg. 3)

on the same page, to report (I have slightly edited the text):

[C]hanges can be blamed on the general economic slowdown and the Land and Buildings Tax that takes [continued] effect in early 2020. There is a lot of new land coming up for sale as owners gear up for the [further rise in the] tax next year.

CBRE *[a Thailand consulting firm] noted that there is an increasing number of landowners with large tracts of land for sale. They say that owners, affected by the slowdown in the country's economy, are offering up slices of Bangkok land and properties with "negotiable deals or flexible prices."*

Photo by Geoff Greenwood on Unsplash

Worried about the upcoming Land and Buildings Tax, some owners are trying to divest themselves of some of their property assets. Some landowners are also offering leasehold options to minimize new costs from the new tax.

The new Land and Buildings tax will tax vacant land at .3 – .7%, with a rise of .3% every three years. To put that into perspective, for a one-rai vacant plot on Phloenchit Road, Bangkok, the tax rate will be 2 million baht per year. (1 *rai* = 0.29 acres)

New appraisal prices for land take effect for four years starting from Jan 1, 2020. According to the Treasury Department, the revised appraisals will mean an average increase of 2.5% in Bangkok and 8.3% *nationwide.*

According to CBRE, *with so many plots coming onto the market at more negotiable prices, land prices in Bangkok could drop by 5-10% from last year or at least remain flat, for the first time since* 2009. *CBRE reports that the average increase in land prices across Thailand per year has been around 2-3%, and 5-6% for Bangkok. But that has accelerated in recent years with land prices in Bangkok rising more than 10% per year over the past couple of years.*

[Another consulting firm] says that the 'sellers' market is now turning into a 'buyers' market around Bangkok.

"We're still seeing a steady surge of buyers, both local and international, but the heat from the last couple of years has cooled, and that's a good thing."

This is a signal victory for proponents of land value taxation. It adds one more country to the list of places in the Eastern Hemisphere, where land value taxation is now employed. These countries include Australia, Hong Kong, Singapore, and Taiwan. South Korea, which has a strong Georgist network, may soon follow in implementing a land value taxation policy.

The Economics of Land Use Controls
(cont'd from pg. 3)

Land developers are sometimes required to build streets and other infrastructure as a condition of being allowed to build a new subdivision, but this practice does not go so far as to include a regulatory means by which people who want to make changes in land use are required to pay for the costs of the changes that they want to make.

From an economic perspective, an ideal system of land use controls would be one that charged every user of land for the harm their land use caused those who used surrounding land, and that would also give each land user a cash credit for the benefit of their land use to those using surrounding land. It would be easier to create such a system of land use controls in a society in which, as Henry George advocated, all or nearly all of the rental value of land was collected. Such a system could work as follows:

The land assessor in each locality would determine the rental value of each parcel of land; they would also determine the monetary value that the use of each plot of land would add to or subtract from the rental value of surrounding sites. This determination would be compared to the alternative of fencing off the land and preventing all human use. These assessments would not be detailed inquiries, property by property, but rather generalizations based on statistical studies; the underlying rental values would be estimated on a steady curve whose peaks represented where rents were known to be highest. The local government would then collect a tax equal to 90% of base rental value plus 100% of harmful consequences minus 90% of beneficial consequences.

If the holders of title to land were compensated for the publicly beneficial effects from their land usage, this would tend to raise the rental value of land in an immediate and direct way. If the holders of title to land had to pay for the harmful consequences of their land usage, this would raise rental values indirectly: When someone was charged for a harmful consequence, the corresponding penalty payment would offset the reduction in rental value elsewhere. That the land title holder was willing to pay would evidence that his property was made more valuable by the opportunity to act in a harmful way and pay the penalty than it would have been by regulatory prohibition of this action. When a land title holder refrained from a harmful act because of the ensuing penalty payment, it would demonstrate that such an action would not have been worth the harm it caused; this forbearance would thus keep total land rents higher than they otherwise would have been.

While such adjustments to rental value take appropriate account of the on-going consequences of land value uses, there are effects from changes in land value for which they do not account. A change in land use tends to change the optimal use of surrounding land. This can cause the obsolescence of surrounding buildings more quickly, and therefore a loss in value. It also tends to change the demographic of residents and businesses that would optimally occupy the area, which generates moving costs for current residents and businesses. To compensate for these costs, there should be one-time payments to the building owners, the residents, and the businesses that are renting space in the area.

I propose the following procedure for dealing with these costs. The party wishing to make a change in land use would propose a total compensation amount for the building owners, the residents, and business owners in the area. Then the land use administrator would allocate shares in the proposed compensation to the affected parties, according to her best estimate of their relative costs. There would then be a vote of the affected parties, with votes weighted by their assigned shares of compensation. If 60% of the shares voted that the compensation was adequate, then the proposed land use change would be approved and the compensation would be distributed. Otherwise, the proposed land use change would be disapproved.

One land use issue that the proposed system does not address is the tendency of localities to disapprove the construction of multi-bedroom apartments, due to the consequent increase in school costs when families with multiple children move into those apartments. The land use administrator can correctly say that the need to pay for the educations of the children who would live in the proposed apartments would raise everyone's taxes and be likely to lower total property values. We say that we believe in public schools, but we are not happy with the prospect of paying for the schooling of all the children who would move into our communities if there were no constraints on building housing for them. To deal with this difficulty, we would either need to say that land use administrators were not allowed to count the cost of providing services for new residents as a harm charged to a proposed change in land use, or we would need to find a source of financing education other than taxes on those who live in the same community as the children to be educated.

To reiterate what was previously stated: one purpose of land use controls is to prohibit uses of land that are detrimental to both the public and/or the land itself and to prevent the effects such inappropriate land use can have on people who use the land surrounding a particular property. Current systems of land use controls have significant limitations as to their effectiveness. A more economically efficient system of land use controls would charge people for the harm incurred from land use and credit them for the beneficial effects of land use, both on an on-going basis of evaluation. There would also be a one-time charge for changes in land use. Some further reform would be needed to deal with the reluctance of communities to allow the construction of housing for low-income families.

The Minneapolis 2040 Plan Is Unlikely to Provide Affordable Housing (cont'd from pg. 4)

Now that we know that, in fact, the Minneapolis 2040 plan will not lead to a building boom, why should we be skeptical of its housing plan on theoretical grounds?

First of all, "upzoning," as the Minneapolis 2040 plan calls for, does not work, and for counter intuitive reasons. Sure, adding more housing to a city with a fixed area should make shelter cheaper. Yet, in reality, this isn't how attempts to expand affordable housing have worked. The greatest challenge isn't in adding more units, but in adding the right kinds of units, at the right costs, and for the right people. Creating housing is easy, but creating it for the poor is not.

Relying on the established norms of land economics, developers will buy up real estate, build fairly expensive buildings, and the neighbors will benefit from the spillovers of higher land values. Poor households will not be able to afford the new residences. In fact, it may be even worse than this: One study in Chicago, Illinois found that after five years upzoning increased property values without expanding the housing supply.

So what approaches can cities try as effective alternatives to upzoning?

Fundamentally, if upzoning alone doesn't pay to house the poor, then the solution is to make it pay. One recent discussion paper found that the best option was to make "inclusionary zoning" more efficient. (The Minneapolis 2040 plan does have some inclusionary zoning provisions, but they're negligible.) Inclusionary zoning is a series of regulations that require developers to set aside some amount of space in their new properties for below-market rental units. Would-be residents would participate in a lottery and then meet an income qualification threshold. Inclusionary zoning could be made more efficient by reducing that threshold and requiring tenants to requalify every few years, in order to keep lower-income households in the units.

The trick, though, is making inclusionary zoning affordable. Developers, who want to build expensive housing for high-income residents, claim it isn't economical to set aside units for below-market tenants. If their criticism is correct, then one option U.S. urban planners can look at, to the extent their state governments allow it, is to abate the building tax on new structures for a certain period of time, or, ideally, to eliminate it altogether.

One city facing a housing crisis took this approach: New York City in the 1920s.

Back then, New York City allegedly had a 0 percent vacancy rate and rents were sky high. Governor Al Smith signed a law that modified the state's property tax system largely in the manner discussed above. The results were dramatic: New York City rapidly built new housing, and the city's population grew even during the Great Depression, in the following decade, when housing growth in other regional cities stopped. It does not appear that inclusionary zoning played any role in the law's land-value taxation system. Interested readers can learn more by reading economist Mason Gaffney's essay, "New Life in Old Cities."

Like most other states, Minnesota property-tax law does not authorize municipalities to treat buildings differently from the land they sit on, but there is a bill before the Minnesota House of Representatives that would permit them to do so. Consequently, Minneapolis lacks the legal authority to make the Minneapolis 2040 plan work better . If the plan does falter, as I predict it will, maybe housing advocates should look back to the last century for guidance.

Photo by Gregory Hayes on Unsplash

Minneapolis skyline at dusk