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URBAN REVITALIZATION IN IOWA

Gretchen Hayne
Dan Johnson
Douglass B. Lee, Jr.

THE LEGISLATIVE ENVIRONMENTAL ADVISORY GROUP

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THE INSTITUTE OF URBAN AND REGIONAL RESEARCH, UNIVERSITY OF IOWA

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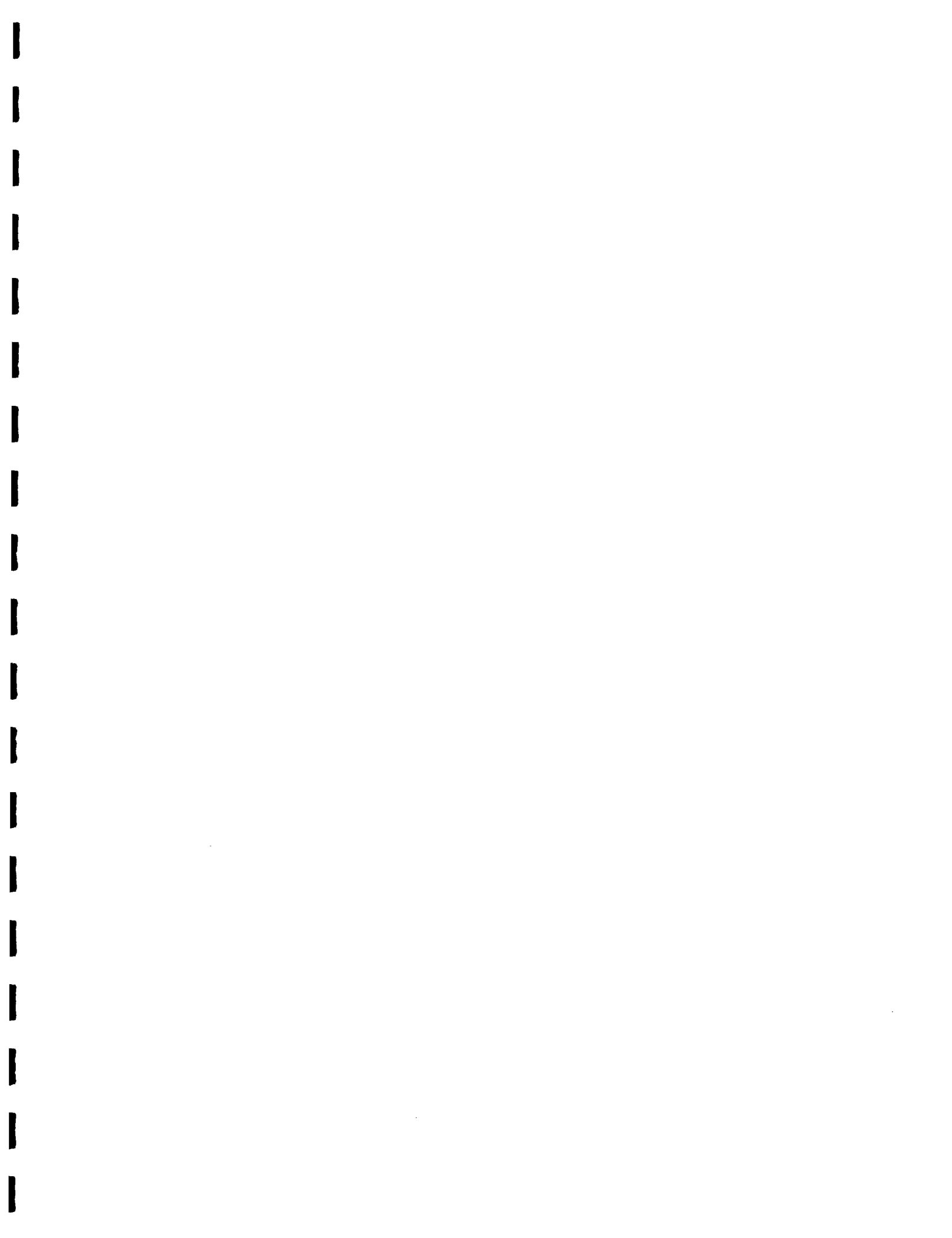
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Ms. Hayne and Mr. Johnson are students in the Graduate Program in Urban and Regional Planning, University of Iowa. Dr. Lee is Chairman of the Graduate Program in Urban and Regional Planning.

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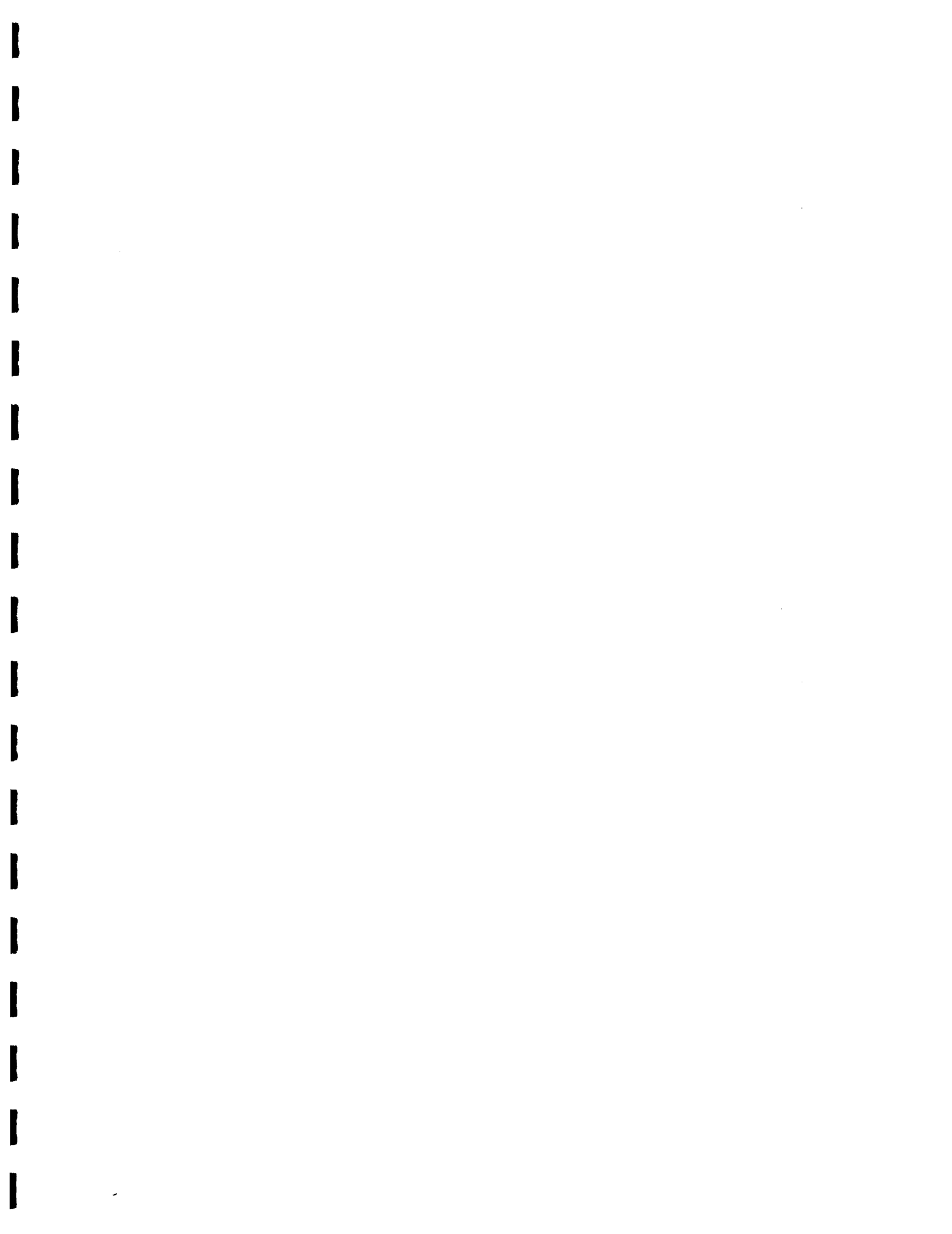
PREFACE

The Ford Foundation Program in Policy Analysis for State Environmental Management is providing support for land use research in Iowa. This program is designed to increase involvement of college and university researchers in public policy research.

In Iowa, the Legislative Environmental Advisory Group (LEAG), consisting of legislators, university faculty and representatives from state agencies and local government associations, was formed to: 1) foster dialogue between policy makers and researchers, 2) solicit and fund college and university based research projects related to land use in Iowa, and 3) transmit research results and technical analyses to all members of the Iowa General Assembly.

Under the direction of LEAG, the Institute of Urban and Regional Research, University of Iowa, solicited research proposals and, as a result of this solicitation, six research projects were completed in 1978. The purpose of these projects is to provide background information and technical analyses to better understand the effects of existing or proposed policies. Project reports are now available for distribution and are listed on the back page of this report.

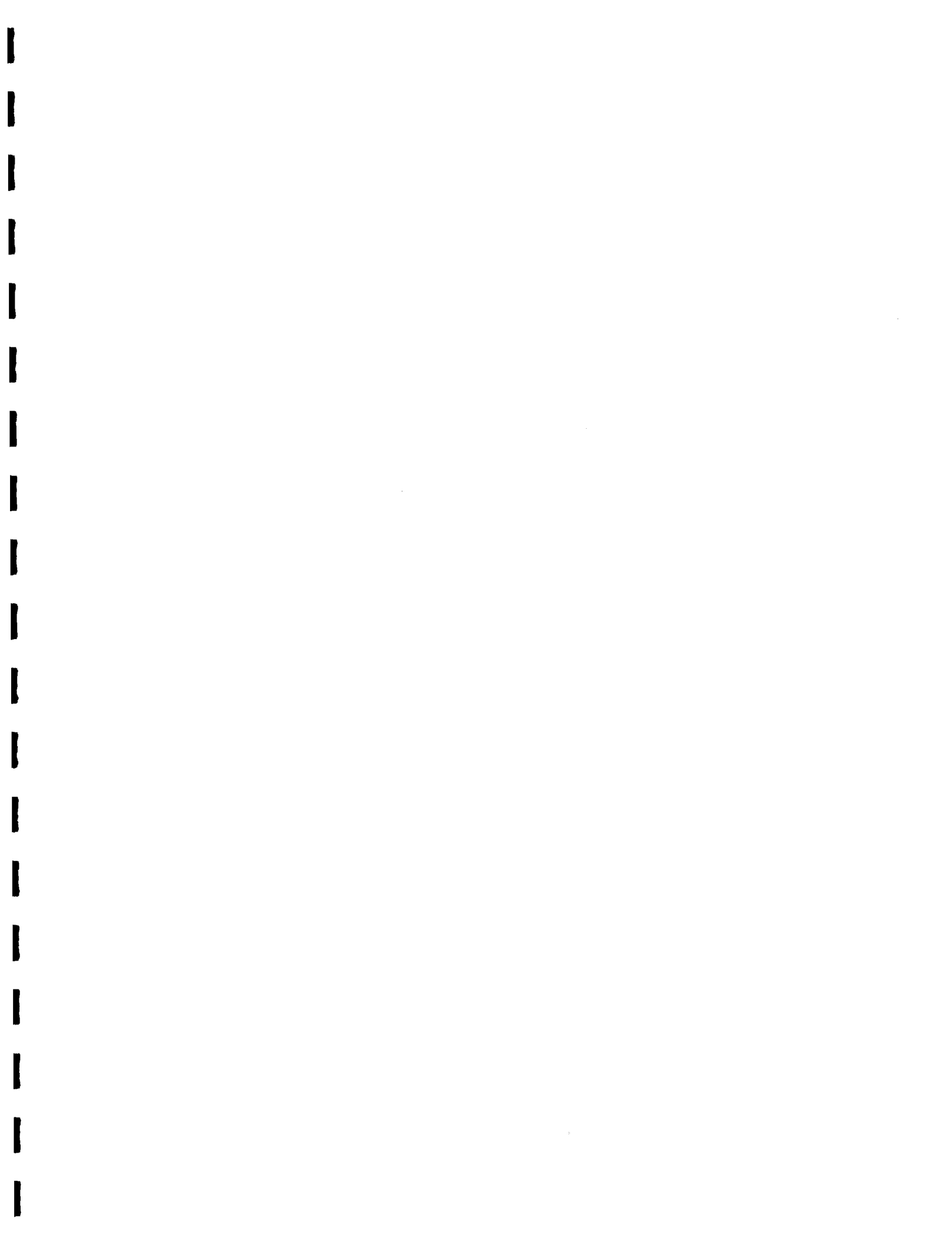
Kenneth J. Dueker, Director
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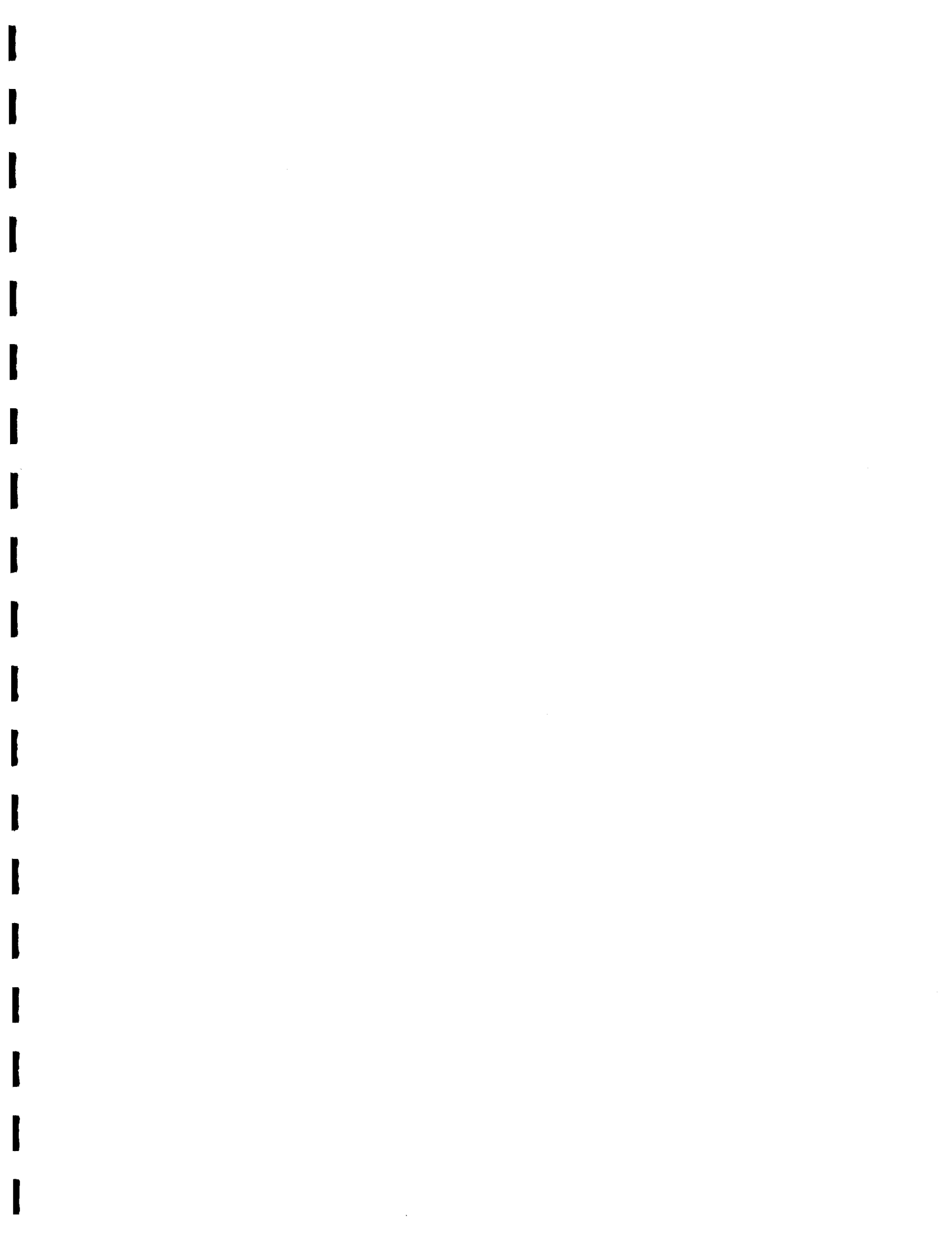
This study was undertaken in response to a request for proposals from the Legislative Environmental Advisory Group. Three major tasks were involved in the project: 1) a survey of actions taken by all levels of government, as well as the private sector, that might fall under the heading of urban revitalization; 2) an analysis and evaluation of the features contained in recently proposed Iowa legislation; and 3) a review of public policies (designed for other purposes) that tend to work against urban revitalization. Most of the first task, which was carried out by Ms. Hayne and Mr. Johnson (graduate students in Urban and Regional Planning), is presented in the second section of the report. Responsibility for the analysis of economic incentives in the current bill is mine, and the remainder of the report is the result of joint efforts. We benefited from discussions with legislators at two meetings of the Interim Study Committee on Urban Revitalization (Robert Bina and Fred Nolting, co-chairmen), and are grateful for the opportunity provided to discuss our preliminary findings with that group. Also of considerable help was a meeting of the Iowa Chapter of the American Planning Association (Jerry Knox, Iowa State University, President), which brought together many professionals, officials, legislators, and academics from around the state to spend a day going over the proposed legislation. Specific individuals who gave us a great deal of time and information--especially on details and sources of information--include Dave Long of the Iowa League of Municipalities and Jim Conway of the Davenport Downtown Development Corporation. My enjoyment of this project was much enhanced by the enthusiasm, interest, and cooperation of all of those with whom I came in contact, not least of which were my two diligent research assistants.

Douglass Lee
Principal Investigator



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SUMMARY AND CONCLUSIONS

As in many other states, interest in urban revitalization has become strong in Iowa in the last few years. That this should be true in Iowa, a relatively non-urban state, may be surprising, but the definition of "urban" in this report is intended to include all 955 municipalities in Iowa. The aim of urban revitalization is to encourage the extended use of structures and community facilities in existing towns and cities, as opposed to further development on agricultural land and in the limited number of wooded and natural areas of the state.

A wide range of public programs and policies that affect urban revitalization are surveyed in the next section of the report, including programs at federal, state and local levels. The following section directs attention at measures voted upon in the Iowa General Assembly during the 1978 session, as modified by the Joint Interim Study Committee on Urban Revitalization, and evaluates rely primarily on tax exemption for property improvements and the extension of credit through revenue bonding to private revitalization efforts, as incentives to reinvestment. The final major section of the report assesses the counterincentives to revitalization, primarily in the form of subsidies to urban development on fringe and rural land.

With respect to the Iowa legislation, we found that:

- (1) The tax exemption measures--essentially an exemption on property taxes on new improvements for ten years--do not create a very strong economic incentive. Even for those properties ideally suited to the provisions of the legislation, an incremental rate of return of 1.5% on the value of improvements is higher than could be achieved in most circumstances. This low monetary return may not turn out to be an important factor in revitalization, and revision in later years to the basic legislation can be undertaken if the economic incentives need to be boosted. Given the magnitude of these incentives, the complicated declining-schedule option offered in the legislation might be dropped.

(2) The stronger economic incentive--industrial revenue bonding applied to residential and commercial as well as industrial property--provides an incremental rate of return equal to the difference between the market rate of borrowing and the interest rate for which the revenue bonds can be sold. Typically, this difference is about two percent.

(3) No direct grants or other state expenditures are contemplated by the legislation, but the tax exemption and revenue bond provisions can be coordinated with and supplemented by other public programs, including Community Development Block Grant (CDBG), urban renewal, code enforcement, Housing Finance Authority, capital improvement, and human services programs. The proposed legislation adds to the existing array of available instruments and programs, giving the localities more flexibility to match specific needs and opportunities.

(4) Estimating the impacts of applying the revitalization provisions to a particular neighborhood is extremely difficult because the factors affecting revitalization are so subtle. Even after the fact, it will be difficult to determine how much investment took place as a result of the program versus how much would have occurred anyway. In general terms, a comprehensive and coordinated set of revitalization instruments applied to a suitable area is much more likely to stimulate new investment than is the simple act of designating an area for revitalization. Hence, the planning requirements in the act should be regarded as an important aspect of any revitalization effort.

(5) Provisions requiring cities to pay relocation payments to persons displaced as a result of a revitalization program will create strong disincentives to revitalization activities that displace residents and commercial activities. Since the municipality will have to provide relocation assistance to all persons in a revitalization area who are dislocated--whether or not the dislocation is a result of the revitalization program--it is unlikely that a revitalization area will be designated which will involve the dislocation of tenants. In fact, unless a city expects

a substantial amount of induced investment (investment which would not have occurred without the revitalization incentives) to take place in a potential revitalization area, the city will be discouraged from designating any areas for revitalization because tax base increases will be insufficient to offset tax losses.

(6) Restrictions on rezoning, both before and after the designation of an area for revitalization, probably constitute an unnecessary burden to local decision-making. If the purpose is to prevent the "bulldozing" of neighborhoods in the name of revitalization, then the relocation provisions appear to be a more than adequate mechanism for dealing with this problem.

(7) Given the requirements for public hearings as well as review by the City Development Board, the need for a neighborhood referendum on a revitalization designation appears to be minimal. Such referenda place an additional cost burden on the restricted resources of local jurisdictions and create a substantial impediment to implementation, while gaining only a small amount of protection for the individual property owner or resident. For some issues, residents of cities and counties should look toward the local political process for resolving conflicting interests rather than expecting state-imposed protection at the expense of local autonomy.

As the bill stands now, the requirements imposed on cities as a condition on use of the revitalization incentives probably exceed the attractiveness of the incentives. Experience in other states with similar provisions suggests--although the experience is new and limited--that only a small proportion of cities and property owners actually take advantage of the opportunities when they are available. A bias toward caution may be suitable in an initial phase of policy development, but if the restrictions are so severe that no one uses the legislation, then little is learned about how to improve the legislation in the next round.

SURVEY OF EXISTING FEDERAL, STATE AND LOCAL PROGRAMS

Federal, state and local governments have a long history of involvement in assisting communities in revitalizing neighborhoods and commercial/industrial areas. While each specific program of revitalization is a unique combination of policy measures, common threads run through the numerous programs that have been proposed or are in operation. These common characteristics can be used to generally describe and classify the variety of approaches and mixtures that might be considered. Many programs combine several strategies and purposes, so a single program may be illustrative of more than one characteristic. Table 1 lists examples of programs at each of the three major levels of government (federal, state, local), sorted according to one of the six approaches listed below. Most of these programs, which may affect revitalization either positively or negatively, are described in subsequent sections of the report.

Direct Expenditures: Government funds may be used to encourage activities falling within the scope of desired objectives. Expenditures may take the form of cash supplements, grants, matching grants, low interest loans, or other direct transfers of funds.

Tax Redistribution: All public programs--especially direct expenditure programs--have some redistributive effect, in that revenues are drawn from one set of sources and expended on another set. A few programs, however, neither raise revenues nor make expenditures, yet they have a direct effect on redistributing revenues. One example of this is metropolitan tax base sharing.

Tax Expenditures: Another form of direct financial incentive to the beneficiary, but one which does not require an outlay of public funds, is a tax reduction based on conditions associated with the taxpayer. Tax exemption for improvements or an investment tax credit for businesses are examples of tax

Table 1
Examples of Programs Affecting Urban Revitalization

	Federal	State	Local
1. Direct Expenditures	<p>HUD: housing assistance payments, housing rehabilitation, elderly housing, public housing mortgage insurance, urban development action block grants, urban renewal, home ownership interest rate subsidies, relocation assistance</p> <p>EDA: regional development program</p> <p>Farmers Home Administration: rural housing programs, rural water programs</p> <p>EPA: sewage treatment and sewerage extension grants</p> <p>Small Business Administration grants and loans</p>	<p>Highway aid, transit grants, relocation assistance, per capita monies, municipal and county assistance, school aid</p>	<p>Matching grant programs (e.g., urban renewal), land banking, urban service pricing (e.g., water, sewers), infrastructure and site improvements</p>
2. Tax Redistribution	<p>Lagging regions program</p>	<p>Tax base sharing, assessment equalization</p>	<p>Site value taxation</p>
3. Tax Expenditures	<p>Tax exemptions (state and local taxes, interest payments), capital gains preferential treatment, investment tax credit</p>	<p>Agricultural tax preference, homestead exemption</p>	<p>Industrial revenue bonds, other tax exempt bonds, tax exemption or abatement</p>
4. Regulation	<p>Mandatory federal codes, anti-redlining regulations, grant program regulations, antidiscrimination</p>	<p>Mandatory state construction codes, anti-redlining, requirements for relocation assistance, anti-discrimination, zoning.</p>	<p>Rent control, rent increase limits, code enforcement</p>
5. Grant of Authority		<p>Historic district formation, home rule provisions, tax assessment discretionary authority (differential assessment), regional development commission, urban renewal enabling legislation</p>	<p>Neighborhood government</p>
6. Information/Communication/Organization	<p>Joint development, technical assistance</p>	<p>Housing finance agency, lobbying for increased share of federal urban programs, planning assistance, Housing Finance Authority</p>	<p>Consortium of banks for lending in high risk areas, community development corporation, financial advisory committees, planning assistance</p>

expenditures. The difference between a tax expenditure and a direct expenditure is slight, since a tax expenditure leads to either (a) lower overall expenditures (so that someone fails to receive something they would have without the tax expenditure) or (b) other taxpayers must contribute more in order to make up for the revenues not contributed by the favored taxpayers.

Regulation: Private or public activities may be constrained by standards or guidelines issued by a legislature or government agency. In general, regulations can be used to prevent undesirable actions but they seldom create inducements for desirable actions.

Grant of Authority: One level of government may give permission to another level or to private organizations (e.g., firms) to engage in an activity previously prohibited to that government or organization. Home rule provisions are common examples. Local governments may be given selected powers (e.g., to levy taxes differentially under limited conditions) to use at their discretion; a similar effect may be achieved by clarifying powers where they are unused because they are ambiguous.

Information/Communication/Organization: A final type of policy strategy is to provide relevant information to persons who can make use of it but do not do so without help or encouragement. Forming consortiums of lenders to share in a high risk pool, lobbying for changes at another level of government, clarifying options for potential investors, etc., can affect urban revitalization but do not necessarily involve the types of policy instruments listed above.

FEDERAL PROGRAMS

The majority of programs which involve direct expenditure of public funds to stimulate revitalization are found on the federal level. These programs are summarized below.

U. S. Department of Housing and Urban Development (HUD)

1. Community Development Block Grants. The Community Development Block Grant Program was authorized by the Housing and Community Development Act of 1974 and revised in 1977.¹ A recent summary of this legislation suggests that it was a reaction "to the many criticisms of earlier federal programs, such as urban renewal and model cities. (In effect) the federal government combined all of the funds from these 'categorical' programs into one direct 'block grant' to each participating city. (Recent revisions created a 'Small Cities Program' through which discretionary grants are distributed to communities not included in SMSA's.) As a whole, the local programs must benefit low and moderate income persons, who are defined as persons with incomes below 80% of the median income of the metropolitan area."² A great deal of discretion is allowed in determining how these funds will be spent. The most common uses of CDBG monies have been for physical development programs, including public works, housing rehabilitation assistance, technical assistance, code inspection, demolition, acquisition, relocation, rehabilitation of neighborhood facilities, and neighborhood business district revitalization. The current funding for community development grants is \$3.7 billion, which represents a slight increase compared to prior authorizations.³

2. Section 312 Rehabilitation Loan Program.⁴ The Section 312 Program is designed to make loans to property owners for purposes of rehabilitation at an interest rate of 3%. The loan term is up to 20 years or 3/4 of the remaining economic life of the structure as determined by a HUD appraisal. The maximum loan may not exceed

¹42 USC 5301 et seq., CDBG Regulations, 24 CFR 570 et seq., HUD Notice 6500.

²Community Development Block Grants and Neighborhood Revitalization, Citizens Housing and Planning Association, Boston, MA, August 1978.

³Community Planning Report, Vol. IV, 35, p. 334, October 2, 1978.

⁴Housing Act of 1964, Rehabilitation Financing Handbook, HUD 7375.1 Revised.

\$27,000 per dwelling unit or an amount equal to the "as is" appraisal plus the cost of rehabilitation. Structures rehabilitated must meet all local applicable codes. Section 312 loans may be made in Urban Renewal Areas, Community Development Block Grant target areas and Urban Homesteading areas. The current funding level of this program is \$230 million.⁵

3. Section 8 Rent Assistance Payments.⁶ The Section 8 program is a rent subsidy plan intended to promote the availability of decent housing for lower income people, by providing incentives for the construction, rehabilitation, and allocation of housing for them. Based on the assumption that a family or individual should not have to pay more than 25% of adjusted income for housing costs, HUD subsidizes the difference between that portion and the "fair market rent" of approved units. The program can be used to subsidize rents in existing, rehabilitated, or newly constructed units. It is frequently administered by a state or local housing authority which has additionally been empowered with state enabling legislation to acquire or construct housing units for lower-income households. However, Section 8 subsidies can be, and frequently are, granted directly to private developments which are financed with either FHA-insured or conventional mortgages.

4. Urban Development Action Grants.⁷ Four hundred million dollars a year has been authorized for the three-year Action Grant Program, with \$100 million a year set aside for small communities. Eligible activities include land clearance, site improvements, providing infrastructure, rehabilitation, building public, commercial, industrial and residential structures, equity

⁵Community Planning Report, Vol. IV, 35, p. 334, October 2, 1978.

⁶U. S. Housing Act of 1937, amended by Title II of Housing and Community Development Act of 1974. Section 8 Housing Assistance Payments Program, HUD Handbook 7420.2.

⁷Section 110 of Title I of the Housing and Community Development Act of 1977. 24 Code of Federal Regulations (CFR) Part 570, Subpart G.

funding, loans, loan guarantees, lease guarantees, and other activities. In general, a community must demonstrate that it has the capability of providing housing and employment opportunities for low and moderate income persons. In addition, the city must demonstrate that it is experiencing physical and economic distress. The major purpose of the program is to stimulate joint public-private involvement in dealing with local problems. "Ideally, HUD will be looking for projects which generate substantially more private commitments than the Action Grant money requested." The applicant must "provide evidence through letters-of-intent or legally binding commitments that the private sector will participate financially in the project."⁸ As Eugene Jacobs, the incoming head of the UDAG program, states, "It will only be possible for communities to get results by saying to HUD, 'I need this much,' not 'How much will you give me?'"⁹ HUD has reportedly compiled a list of cities in Iowa which may be eligible for UDAG funds.

5. Congregate Services Program.¹⁰ HUD's recently developed Congregate Services Program has been funded on an experimental basis. This program may be of special interest to Iowa in view of the fact that the state is among the leaders in the nation in providing services to the developmentally disabled. Although specific information is not readily available, it is known that this program will provide assistance in establishing small group homes with subsidized rental rates for individuals who meet certain legally defined criteria of disability.

6. Other HUD Programs. A wide variety of additional HUD programs have been available in the past. Future uses of these

⁸The Action Grant Book, U. S. Department of Housing and Urban Development, May 1978, HUD-488-1-CPD.

⁹Urban Land, Vol. 37, No. 7, July-August 1978, p. 20.

¹⁰Community Planning Report, Vol. IV, 35, p. 334, October 2, 1978.

programs depend on the degree to which they are funded, which has varied greatly in the past. Such programs (from the National Housing Act) include:¹¹

- ** Section 202: Direct loans for new construction of elderly housing, at the going federal rate of interest.
- ** Section 235: FHA mortgage insurance and interest subsidies for lower income purchasers of single-family homes or condominium units. Going rate may be subsidized down to approximately 3%.¹²
- ** Section 213: Mortgage insurance for cooperative housing.
- ** Section 220: Mortgage insurance for rental housing in urban renewal areas.
- ** Section 221: Mortgage insurance for housing (rental, co-op, or home ownership) for low and moderate income families and displaced families.
- ** Section 231: Mortgage insurance for rental housing for the elderly and handicapped.
- ** Section 234: Mortgage insurance for condominiums.
- ** Conventional Public Housing: Federally guaranteed bonds of a local housing authority to finance development of low-rent housing. Annual contributions equal to all principal and interest payable against the project's debt.
- ** Neighborhood Housing Services Program (NHS): Technical services coupled with private endowments; administered jointly with the Federal Home Loan Bank Board.

Farmers Home Administration (FmHA)

In addition to HUD, the Farmers Home Administration administers several rural housing programs. Located in the Department of Agriculture, these programs cover rural areas including cities up

¹¹Financing Options for Development of Housing, San Francisco Redevelopment Agency, September 1976.

¹²HUD Homeownership Subsidy Program, Fact Sheet, HUD-419-HPMC(2), June 1976.

to 20,000 population not in an SMSA and having a serious lack of mortgage credit. These programs include:¹³

- ** Section 504: Rehabilitation loans and grants. For minor improvements on existing single-family rural homes and farms; loan terms up to 20 years; maximum loan amount \$5,000 (1974).
- ** Sections 514 and 516: Domestic farm labor loans and grants. Insure loans to cover up to 90% of housing development costs.
- ** Section 515: Direct and insured loans for elderly and low-moderate income housing. Multi-family rental housing with additional assistance payments to sponsors for very low income families.
- ** Section 524: Housing site loans at going federal rate of interest for acquisition of land as housing building sites.
- ** Other programs include self-help housing, weatherization and Section 8 rental assistance payments.

Economic Development Administration (EDA)

Established by the "Public Works and Economic Development Act of 1965,"¹⁴ the Economic Development Administration (EDA) has concentrated 75% of its activities in rural areas to alleviate hardship among those suffering from severe unemployment. Authorized programs which may have significance for urban revitalization areas were recently summarized by a report of The National Economic Development Law Project.¹⁵ The programs include:

¹³Comparative Elements of Federally-Assisted Housing Programs, NAHRO, Guide for Preparation of a Local Housing Assistance Plan, September 1974.

¹⁴Pub. L. 89-136 (Aug. 26, 1965), 79 Stat. 552; now 42 U.S.C. §3121 et seq.

¹⁵New Directions for EDA, Economic Development Law Project Report, Vol. VIII, Issue 3, May/June 1978, pp. 24-25.

- ** Public Works Grants (Title I): Enable a state, political subdivision, Indian tribe, public or private non-profit corporation to acquire and develop public works and development facilities.
- ** Public Works Loans and Loan Guarantees (Title II): Assist in the financing of public works, public services, and development facilities.
- ** Section 7A Loan Guarantee and Loan Program: Guarantee of up to 90% (\$500,000 maximum) of a loan made by a private lender and/or a direct lower interest loan of up to \$150,000 by SBA. Loan period is six years for working capital, ten years for equipment, twenty years for new construction.
- ** Section 502: Loan of up to 90% of financing needs, for up to 25 years, from a Local Development Company (LDC) which is funded by an SBA loan or loan guarantee. Seventy-five percent of the LDC's voting power must be controlled by persons residing or doing business in a "target area". Limited to \$500,000 for each small business.¹⁶

Other National Programs

Other federal and national programs which can have a significant impact on urban revitalization projects but which cannot be fully discussed within the limits of this study include:

- ** EPA sewage treatment and sewerage extension grants.
- ** Urban renewal.
- ** Historic preservation.
- ** Location and financing of federal facilities.
- ** Anti-redlining regulations.
- ** Comprehensive Employment Training Act (CETA).
- ** Federal tax policies (e.g., 10% investment tax credit on at least 20-year-old commercial and industrial buildings).
- ** Numerous programs of the Departments of Health, Education and Welfare; Labor; Interior; and Transportation (e.g., ground transportation centers).
- ** Private national endowments, foundations, and philanthropic organizations (e.g., Ford Foundation).

¹⁶From Massachusetts Governor's Conference on Community Revitalization, Massachusetts Office of State Planning, May 25, 1978, pp. 22-23.

New Proposals

Several new programs or extensions of existing programs already operating at the federal level have been considered in 1978. One of the more significant statements of proposed policy is The President's National Urban Policy Report of 1978.¹⁷ Recommendations in this report include:

- ** Use of the Community Reinvestment Act to increase the availability of credit to urban home buyers.
- ** Investigation of "public land banking."
- ** Developing coalitions of financial institutions to make market rate loans available in distressed areas.
- ** Metropolitan tax-base sharing where a portion of the increase in non-residential property tax is shared by local governments with the metropolitan area.
- ** Site-value taxation where under-assessed land and over-assessed improvements are reassessed.
- ** A recommended \$2.2 billion increase in the Community Development Block Grant Program with greater preferences extended to older, declining cities.
- ** A recommendation to double the funding for the Section 312 Program.
- ** Increases for UDAG and EDA Title IX programs.
- ** Creation of a consumer cooperative bank to provide financing to members who have difficulty getting conventional financing.
- ** Amendments to the federal tax code to reverse the tendency toward urban sprawl.
- ** Targeting of tax-exempt industrial revenue bonds to distressed areas only, and provisions for credit and other financial incentives for businesses to invest in distressed cities.
- ** A differential investment tax credit of 5% to 15% (structures and equipment) to firms who expand into economically distressed areas.
- ** A targeted employment tax credit to encourage employers to hire disadvantaged young or handicapped workers.
- ** A request for \$1 billion for a program of labor-intensive public works targeted to communities with high unemployment.

¹⁷The President's 1978 Nation Urban Policy Report, U. S. Dept. of Housing and Urban Development, August 1978, 147 pages.

- ** A state incentive grant program in HUD to provide \$400 million over two years to assist states in aiding local governments to implement urban assistance plans.
- ** Creation of a National Development Bank with authorization to guarantee investments totaling \$11 billion through 1981 and provide low-cost, long-term financing to be used with the programs of HUD and EDA which would enable certain firms to reduce financing costs by up to 60%.

In short, the President's Report calls for a comprehensive approach in dealing with urban problems and stresses the need for cooperation among all segments of the public and private sectors. Specific emphasis is placed on providing financial aid where need is greatest, encouraging greater involvement of neighborhood associations, providing employment opportunities, devising incentives to attract private investment, reducing incentives to urban sprawl, and encouraging state governments to become more involved as partners in assisting urban areas.

STATE PROGRAMS

1. Highway Aid

Accessibility can be a key factor in determining an area's overall economic health and investment patterns, and the allocation of state highway funds has a direct impact on accessibility. In Iowa, monies for local improvements are distributed to cities based on the ratio of the population of each city to the total population of all cities in the state; funds are distributed to counties based on county area and need relative to that of the state as a whole.¹⁸

2. Transit Grants

Transit assistance serves the same broad purpose as does highway assistance--it contributes to improvements in mobility and accessibility. Funds are distributed in Iowa according to

¹⁸Ch. 312.3, Code of Iowa.

(1) deficit, (2) quantity of service provided, and (3) size and density of service area.¹⁹

3. Municipal and County Assistance

This involves a redistribution of funds collected at the state level to cities and counties. In Iowa, distribution is based on population. These are general purpose funds, allowing localities to make their own decisions as to their use.²⁰

4. School Aid

Quality of education can be a crucial element in neighborhoods undergoing (or attempting to begin) revitalization.²¹ Quality education depends to a large extent on the level of funding. Recognizing the disparities (in terms of quality) that would exist between districts were education financed entirely through the property tax, the state may attempt to equalize educational opportunity through its school aid allocation procedure. This is the purpose of Iowa's allocation procedure, where the local school district's state share of the cost of public education is determined by the ratio of its property value to that of the entire state, together with the ratio of its income to that of the entire state.²² The allocation of funds within districts is equally important in terms of neighborhood revitalization.

¹⁹David Forkenbrock and Kenneth Dueker, "Principles and Application of a State Transit Assistance Allocation Procedure," Technical Report 106 (Iowa City: Institute of Urban and Regional Research, The University of Iowa), August 1978.

²⁰Municipal Assistance Fund, Ch. 405.1, Code of Iowa; County Government Assistance Fund, Ch. 334A, Code of Iowa.

²¹S. Jerome Pratter and Susan Uchitelle, "The Interrelationship Between Urban Neighborhood Revitalization and Quality of Schools," presented at The National Conference of the American Institute of Planners, September 28, 1978.

²²Chs. 442.9 and 442.10, Code of Iowa.

5. Assessment Equalization

If the average assessment ratio (assessment to market value) is made everywhere equal with expenditure patterns held constant, a redistribution occurs from properties previously under-assessed to properties correctly or over-assessed. A study of property taxes in the U. S. cities found effective tax rates (tax as a percentage of investor reported market rate) to be generally higher in blighted neighborhoods than in other neighborhoods.²³ Since millage rates were uniform throughout each city, the study ascribed the effective tax rate differential to variations in assessment/market ratios between neighborhoods. The implication is that assessment equalization can cause a redistribution to occur from other areas to blighted areas thereby contributing to revitalization efforts. Iowa law requires that assessed value of property in one jurisdiction be equalized as compared with assessed value of property in an adjoining jurisdiction.²⁴

6. Agricultural Productivity Taxation

Used to encourage retention of land in agricultural use, agricultural productivity taxation allows agricultural land to be taxed according to its agricultural income-producing potential rather than on its market value. The expectation is that farmers of land on the urban fringe will continue to profit from farming operations, where they might not were their land taxed on its actual market value. Agricultural productivity taxation can be a disincentive to costly fringe development only if some sort of binding promise can be extracted from the farmer to keep the land

²³Hadi Madjid, A Study of Property Taxes and Blight, Volume 1, report to U.S. Department of Housing and Urban Development, Cambridge: Arthur D. Little & Co., 1973, HUD-PDR-29-3, p. 2.

²⁴Ch. 441.21, Code of Iowa.

in its agricultural use for a specified period of years and if participation in the program is widespread.²⁵

This year, all Iowa farms will be valued entirely according to their productivity. Upon a change in use, the farmer is liable for five years of back taxes comprised of the difference between the taxes that would have been paid had the property been assessed at market value and the taxes actually paid.²⁶

7. Anti-redlining

Redlining refers to the practice whereby lenders withhold mortgage credit from areas perceived as being deteriorated or in the process of deteriorating. This practice can cause, as well as reflect, the decline of a neighborhood. Laws prohibiting red-lining, if properly enforced, can have the effect of halting the process of deterioration before it reaches the point where it can no longer be turned around. Under the recently enacted Iowa law, it is a criminal offense to "knowingly refuse to make a mortgage loan solely on the basis of neighborhood or to make loans on less-favorable-than-usual terms because of prevailing income, ethnic or racial characteristics, or age of structure in the area."²⁷

8. Requirement for Relocation Assistance

The state recognizes that some socially beneficial programs may result in resident dislocation. Requirements for relocation assistance are intended to compensate persons in this situation as well as to ensure that projects are not undertaken when real social costs exceed benefits.

²⁵Gregory C. Gustafson and L. T. Wallace, "Differential Assessment as Land Use Policy: The California Case," *Journal of the American Institute of Planners*, Volume 41, Number 6, November 1975, pp. 379-389.

²⁶Chs. 441.21 and 445.63, Code of Iowa.

²⁷"Disclosure of Redlining," Editorial, Des Moines Register, August 31, 1978, p. 10A.

9. Mandatory State Building Codes

State building codes exist to protect the health and safety of building occupants. Cities are charged with enforcing them. Codes are based upon current standards of construction and sanitation with the result that older buildings are often able to comply only at considerable expense.²⁸ In the extreme case, a property owner may choose to abandon the property rather than to make the required improvements. Counties in Iowa are not now required to adopt building codes.

10. Historic District Formation

Historic districts formed through local zoning or referendum require property owners to submit an application to the Historic District Commission or building permit department before demolishing or altering the exterior of an historic building or for new construction.²⁹ These restrictions are generally aimed at preserving the historic "character" of the district. In addition to the benefits flowing to properties located within the district, surrounding areas may also benefit as a result of their proximity to the historic district.

11. Tax Assessment Discretionary Authority

Differential assessment refers to the practice of taxing land at a higher rate than the buildings situated upon it, or assessing different land uses at differing portions of full market value. High taxes on land relative to buildings theoretically should encourage investment in improvements generally and discourage the holding of vacant land. Pittsburgh's graded tax plan is seen

²⁸Don Borchelt, Community Development Block Grants and Neighborhood Revitalization: A Handbook, (Boston: Citizens Housing and Planning Association) August 1978, pp. 14-16.

²⁹Michael J. Wiedl, III, "The Law of Historic Preservation," Urban Land, July-August 1975, p. 28; also, Ch. 303.27, Code of Iowa.

as having played a major role in the development of that city's Golden Triangle.³⁰ Massachusetts has recently adopted a referendum specifying assessment ratios for major classes of land use. Counties and cities in Iowa are required to assess all real property (except farmland) at 100% of full market value, and levy a uniform tax rate on all properties in the same tax jurisdiction.

12. Urban Renewal Enabling Legislation

Section 403 of the Iowa Code provides a number of measures to cities for use in designated renewal areas.

13. Housing Finance Agency or Authority

State housing finance agencies operate in much the same way as do their federal counterparts by making low interest loans and/or loan insurance for housing available to low and moderate income persons. Loan funds are acquired through the sale of tax-exempt bonds to private investors. Loans are made through participating mortgage lenders, which in turn lend the funds to eligible applicants. The Iowa Housing Finance Authority was created through enabling legislation in 1975. An initial bonding capacity of \$100 million was increased to \$250 million by the 1978 Legislature. The IHFA makes low interest mortgage loans available to low income Iowans for the purchase of homes in any location within the state. In addition, low interest loans are provided for apartment developments for low and very low income Iowans. The IHFA does not insure mortgage loans.³¹

Housing finance authority funds can be used to augment other types of programs. IHFA staff have announced a set-aside of funds to be used specifically within areas designated as revitalization areas, providing the Urban Revitalization Bill is passed by the 1979 Iowa Legislature.

³⁰Williams, "Pittsburgh's Experience with the Graded Tax Plan," The American Journal of Economics and Sociology, 22, 1963, pp. 209-223.

³¹Iowa Housing Finance Authority, Factsheet, November 16, 1978.

14. Special Improvement Districts

Various kinds of public improvements can be constructed and maintained at the expense of property owners that directly benefit from them. Improvement districts can be initiated by the municipality (through Section 384.39 of the Iowa Code) or sometimes on the basis of actions by private property owners (such as Section 386 of the Iowa Code). These financial instruments allow projects to be undertaken for a group of property owners, rather than either a single owner or the city as a whole.³²

LOCAL PROGRAMS

1. Matching Grant Programs

Matching grants function as a price incentive in favor of the aided activity because the locality has only to pay a specified percentage share of the cost of the program; the remaining share constitutes the grant. Matching grants are used to encourage activities viewed as being socially beneficial from both the local perspective and from the wider perspective of the government making the grant. Among the major federal matching grant programs are housing, urban renewal, highway construction, water and sewer construction programs, and public assistance programs.³³

2. Urban Service Pricing

The frequent requirement of average cost pricing as the means of financing the extension of municipal services has been cited as

³²These programs and many others of a special and general nature are described in the Office for Planning and Programming, Downtown Improvement Manual for Iowa Cities (Des Moines: OPP) July 1978.

³³Stephen M. Barry, The Urban Impacts of Federal Policies: Volume 3, Fiscal Conditions (Santa Monica: The Rand Corporation) April 1978, pp. 81-82.

a contributor to urban sprawl.³⁴ Water and sewer networks, gas and electric lines, and roads are examples of such services. Since everyone shares equally in the cost of constructing additional facilities to service new development, areas with existing service networks are forced to subsidize newly developed areas.³⁵ Pricing according to costs occasioned would force fringe development to pay the "true" cost of extending services, but for some services (notably streets) the authority is not entirely clear.

3. Infrastructure and Site Improvements

Basic infrastructure and site improvements can be used as a means of stimulating private investment within an area. In some cases, explicit agreements are made between the city and private developers where the city provides certain site improvements in exchange for development at a certain location. Typical examples include the repaving of streets and sidewalks, replacement of obsolete utilities, installation of street lamps and construction of neighborhood parks.

4. Land Banking

Units of local government may acquire land for public purposes in advance of need, thereby providing for sites for future facilities and guiding growth away from (or controlling it on) those sites. Public funds are required for advance acquisition, and little use has been made of the concept in the U.S.

5. Site Value Taxation

Site value taxation is the extreme form of differential taxation where only the land is taxed and the improvements on it

³⁴Philip M. Raup, "Urban Threats to Rural Lands: Backgrounds and Beginnings," Journal of the American Institute of Planners, Volume 41, Number 6, November 1975, p. 374.

³⁵Ibid, p. 374.

are not. By entirely shifting the emphasis of local property taxes in urban areas from improvements on land to the land itself, there no longer exists a disincentive towards making improvements. Additionally, speculative purchase and leapfrog development on the urban fringe would be discouraged under site value taxation, since taxes on raw land would no longer be less than taxes on developed land.³⁶ Site value taxation is currently being used in Arden, Delaware, and in many cities in Australia and New Zealand.³⁷

6. Industrial Revenue Bonds

Since the interest earned on municipal bonds is tax exempt, municipalities are able to borrow money at lower than market interest rates. Industrial revenue bonds are used to entice industries to locate in an area by passing this interest savings along to them. The city realizes returns in the form of an expanded property tax base and more jobs for residents (leading to better overall economic health).

The Iowa Urban Revitalization Bill (House File 2448), if it had passed, would have expanded the category of eligible recipients of revenue bonds to include residential, commercial, and non-profit projects as well as industrial.³⁸

7. Other Tax Exempt Bonds

Revenue bonds and general obligation bonds are the vehicles by which local governments can borrow money. GOB's are backed by the "full faith and credit" of the city and usually require voter

³⁶U.S. Department of Housing and Urban Development, The President's National Urban Policy Report 1978, HUD-CPD-328, pp. 105-106.

³⁷T. William Patterson and Kumares C. Sinha, "Implementation of Core Area Improvement Programs through Tax Policies," presented to the National Conference of The American Institute of Planners, New Orleans, 1978.

³⁸Iowa Legislature, House File 2448, p. 9.

approval for their issuance. States often impose ceilings on the amount of money that can be borrowed in this manner. Revenue bonds are backed only by the revenues expected to be generated by the project and therefore usually do not require voter approval. GOB's generally have lower interest rates than do revenue bonds because of the lesser amount of risk involved. Both types of bonds carry below-market interest rates because of the tax-exempt status of the interest earned.

8. Tax Abatement and Exemption

Tax abatement refers to the practice of decreasing a property tax liability, while tax exemption prevents or lessens the increase in tax liability that would be occasioned by making improvements to the property. Both are intended to stimulate private investment that would not otherwise occur (see next major section).

9. Homestead Exemption

Homeowners who reside on their property in Iowa are granted a tax exemption on the first \$4,500 of the value of the property. The state makes up the lost revenues for the locality.

10. Rent Controls

Renovation of an urban area may cause rental property owners to raise rents in response to rising property values and tax assessment. Rent controls essentially involve the extraction of an indirect subsidy from the private sector to finance low income tenant relief.³⁹ The other alternative is to use public monies to finance relief. The case for private subsidy is more compelling when property values have risen largely as a result of public investment, rather than private sector activities.

³⁹Dennis Gale, "Neighborhood Resettlement and Displacement: People and Policies," presented at the National Conference of the American Institute of Planners, New Orleans, September 1978.

11. Code Enforcement

Cities are legally required to enforce the provisions of the State Building Code. However, there does exist a wide degree of variation in the level of code enforcement within and between cities. As previously noted, strict code enforcement may impose a substantial burden upon owners of older property, in some cases causing abandonment rather than improvement. Allowance for flexibility in code enforcement may be more consistent with revitalization efforts. Consideration can be given to the amount of financial assistance available and adjustments made in the timing of improvements, the more serious violations being addressed first. Many cities have adopted this approach with results more satisfying than those achieved under the traditional system.⁴⁰

12. Neighborhood Government

Owners and tenants who are affected by revitalization are usually included in some way in the decision-making process. For example, in San Francisco's Rehabilitation Assistance Program (RAP) an elected Citizen's Advisory Committee assists relevant city officials in formulating a development plan and acts as a loan and rent committee to resolve problems which tenants and landlords may have when the program is implemented.⁴¹ Such citizen participation has been essential to the successful operation of the program. Des Moines has delegated some responsibility to elected neighborhood representatives.

13. Consortium of Financial Institutions for Lending in High Risk Areas

Financial pools are formed by private lending institutions to reduce the risk of investing in declining neighborhoods. Risk reduction is accomplished in principally two ways: by spreading the contribution of funds over a large number of firms and by

⁴⁰Op. Cit., Borchelt, p. 15.

⁴¹Rehabilitation Assistance Program Rules, City and County of San Francisco, Department of Public Works, 1977.

investing in the rehabilitation of the area as a whole. Savings and loan associations have formed risk pools to provide mortgage loans in inner city neighborhoods in Washington, St. Louis, Denver, Philadelphia, and many other cities.⁴²

14. Community Development Corporation

Success in urban revitalization is greatest when there exists a working cooperation between the public and private sectors. Community development corporations represent one arrangement through which private/public efforts can be integrated and knowledge and expertise shared. These associations typically include community leaders, merchants, representatives of lending institutions, landowners, developers, local government officials, and other residents.

⁴²Op. Cit., President's Report, p. 94.

EVALUATION OF THE PROPOSED IOWA LEGISLATION

Analysis of the bill proposed in the 1978 session and revised by an interim study committee has been organized under four headings: economic incentives, dislocation and conversion effects, the local decision perspective, and experience in other states with similar provisions. In each topic, a few alternatives not contained in the current version are also evaluated.

ECONOMIC INCENTIVES

The major thrust of the proposed legislation is the creation of economic incentives for private investment through tax exemption and low-interest credit. Tax abatement and tax exemption are often used synonymously, but a difference between these two terms is maintained in this report:

tax exemption: property taxes on new investment are wholly or partially forgiven for some period of time.

tax abatement: taxes are reduced from current levels, i.e., on existing investment.

The Iowa legislation is limited, in this sense, to tax exemption, in that under no conditions does additional investment reduce the taxes on the initial value of the property. Low interest credit would be obtained via extending the use of revenue bonds -- currently available under Iowa law to municipalities for the purpose of industrial development -- to commercial and residential structures in designated revitalization areas.

To estimate the impact of an economic incentive on a private investor (developer or homeowner), the rate of return on the amount invested is the best single summary measure. It is stated in relative terms (a percentage) rather than absolute amounts, and it incorporates a discount factor (i.e., a dollar in the future is less valuable than a dollar now, even after correcting for inflation). The rates of return are incremental, in that they can be added together (e.g., tax exemption plus low

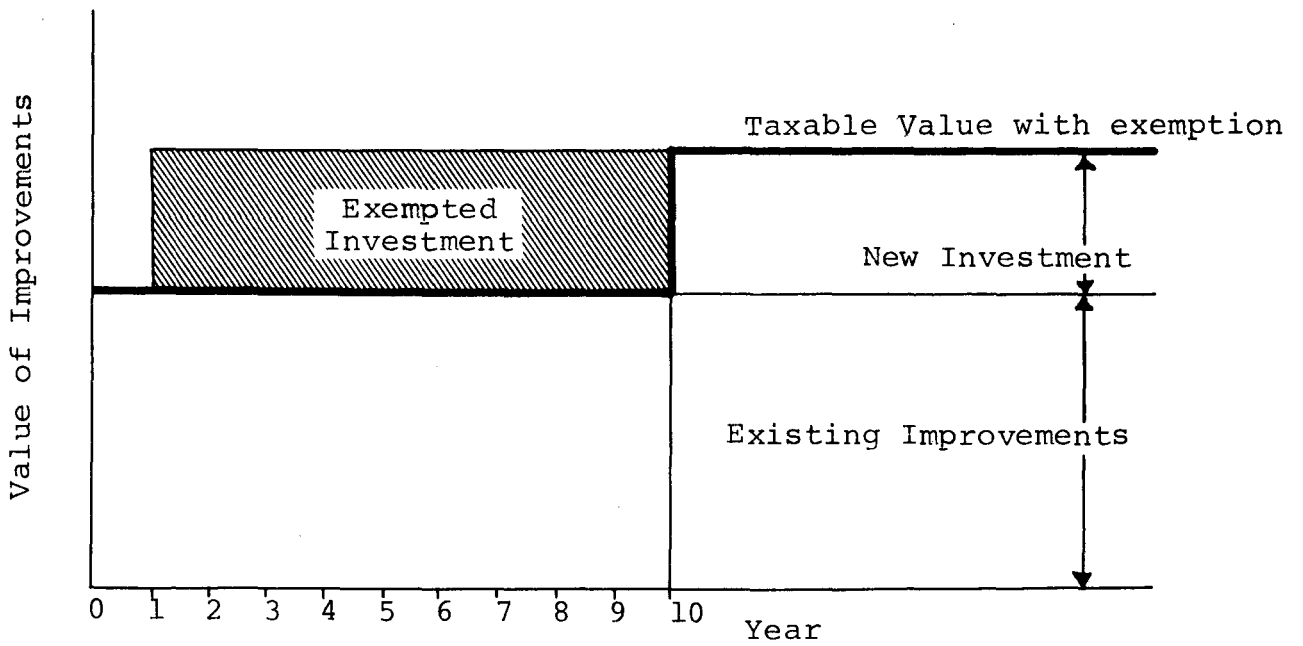
interest loan) and also added to other sources of return on the same investment. A rehabilitation project which would earn 8% for its investor without tax exemption would earn 9% if the tax exemption produced a 1% rate of return.

1. Tax Exemption

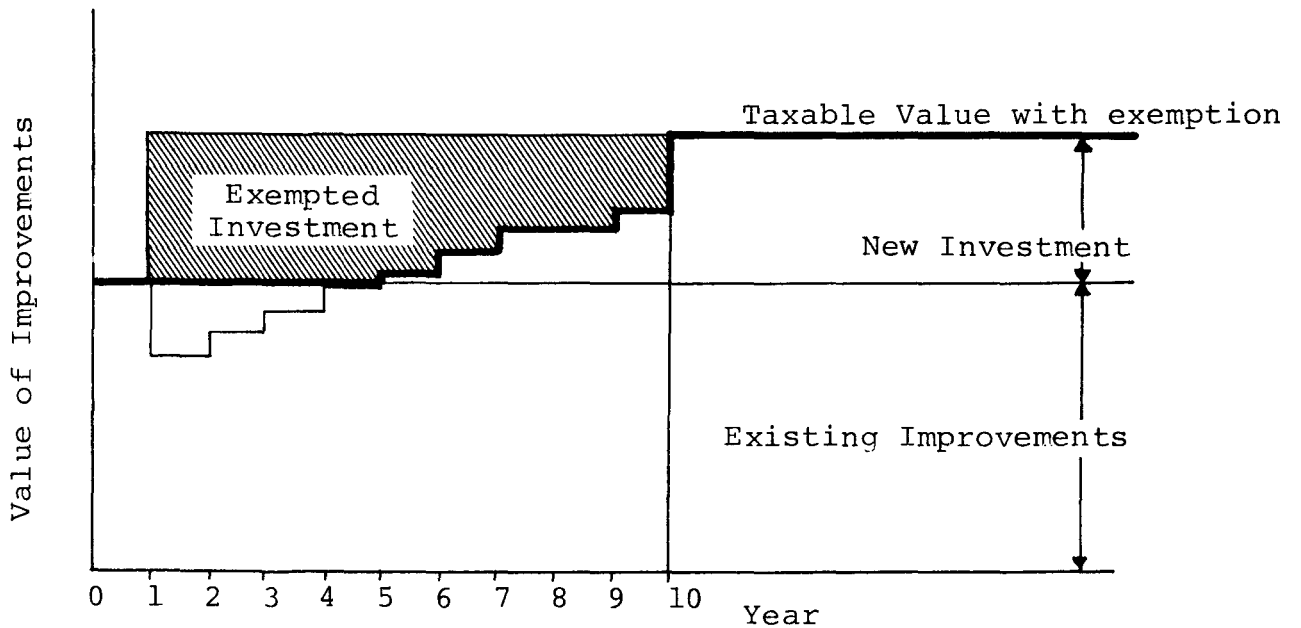
Two options are available, both of which require a minimum threshold investment of at least 15% of the value of existing improvements (not land), and give full or partial exemption for 10 years on the value of the new improvements. Under option (1), exemption is provided up to a maximum of \$250,000 of new investment, for any kind of property, while option (2) provides for a sliding scale of exemption over the ten-year period and is applicable to residential property only, with no ceiling.

The two options can be compared by means of the examples shown in Figure 1. In year zero, the property is in a given existing condition, and investment takes place which increases its value by 50% by the beginning of year one. Under option (1), the value of the property upon which taxes are exempted is the increase in value only, for a period of ten years. Under option (2), a percentage of the total (existing plus new) value of improvements is exempted, ranging from 50% in the first year to 20% in the tenth, but a floor is placed on assessments so that the taxes are only exempted on the new improvements. The schedule is shown by the stepped line in the figure, with the permitted exemption indicated by the shaded area.⁴³

⁴³The height of the stepped line varies depending upon the percentage of new investment: at an increase of 25% or less in value, the line lies entirely below the existing investment level, and the exemption is identical to option (1); for an increase in value of 100% or more, the stepped line lies entirely above the existing investment line. The diagrams assume that there is no inflation and no other change in the value of the property. While the basic concepts are not affected by inflation, it is unclear how the actual working of the legislation will deal with the relationship between assessment practices and inflation, on the one hand, and the exemption floor on the other. If the floor is fixed in dollar terms at the beginning of the exemption period, then appreciation in the value of the property through either



a. Option (1) Tax Exemption on Increased Value for Ten Years for all Types of Property



b. Option (2) Sliding Scale of Exemption for Residential Property Only.

Figure 1. Property Tax Exemption Schedule

The two critical parameters in the rate of return are (a) the effective tax rate (tax paid divided by full market value), and (b) the correct discount rate (the "real" rate of interest). For Iowa, the average effective tax rate is about 2.5% (an amount equal to 2.5% of the full value of the property is paid in taxes each year). The discount rate is harder to determine empirically, but probably falls between 4% and 7% when corrected for inflation. The rate of return is calculated by discounting the future benefits (tax exemption) to a present value, converting that to a constant annual stream of payments, and taking the annual payment as a percent of the investment.⁴⁴ The results are shown in Figure 2.

investment or inflation would tend to make the floor value a smaller and smaller proportion of the total value of the property. Thus, in real terms, the floor would be going down; the base value of initial improvements would remain constant in dollar terms but would be shrinking when adjusted for inflation.

If this description is accurate, the legislation does provide some amount of tax abatement as well as exemption, thereby increasing the rate of return on investment. The amount of this effect will depend upon the rate of inflation in the value of real estate improvements. Rates of return will also be higher if the aggregate return on investment is above the borrowing rate and the investment is highly leveraged.

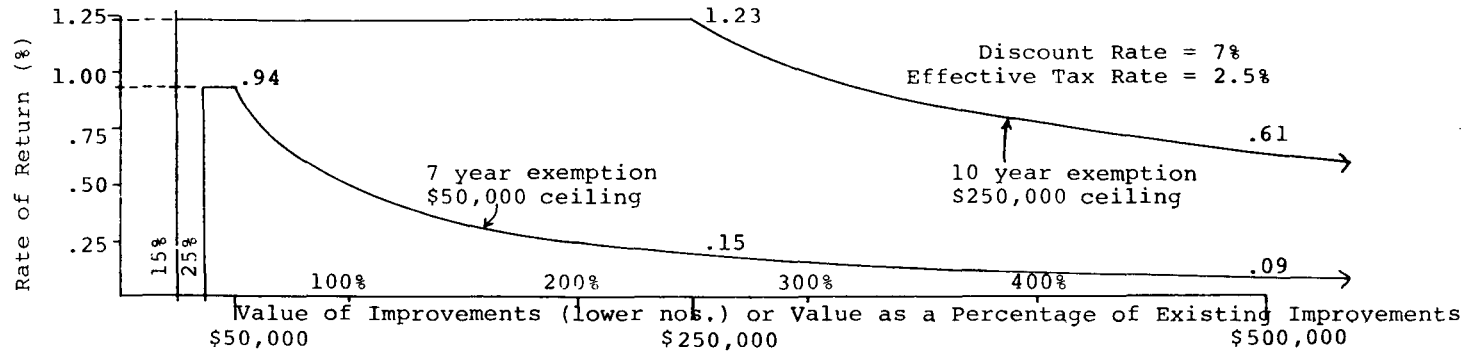
⁴⁴Formally, the rate of return is calculated as

$$ROR(1) = e r \sum_{n=1}^{10} \frac{1}{(1+r)^n} ; .15V \leq v \leq \$250,000$$

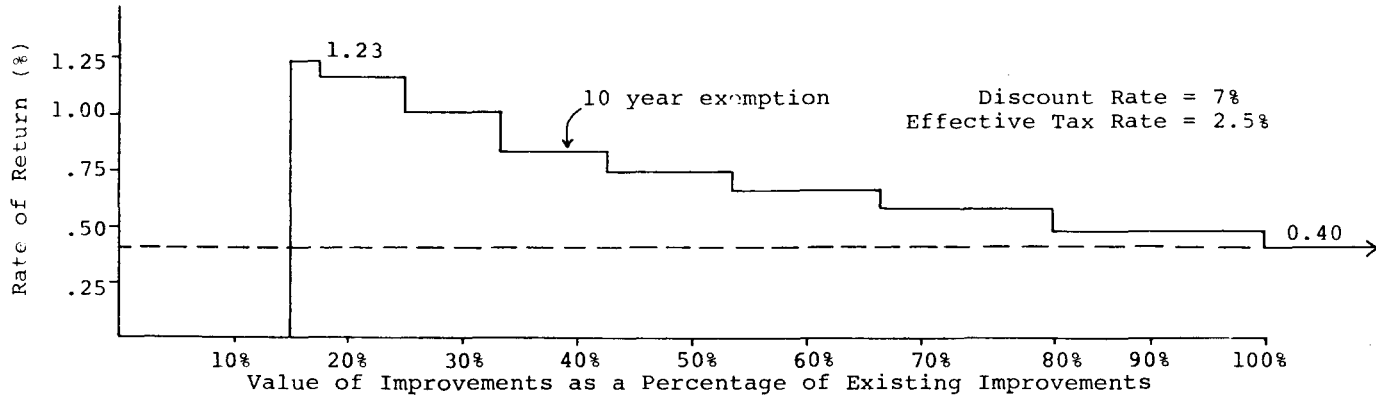
or

$$ROR(2) = e r \sum_{n=1}^{10} \min \left[p_n (V+v), v \right] / (1+r)^n ; .15V \leq v$$

where ROR(1) = rate of return for option (1), e = effective tax rate, r = discount rate, v = value of investment in new improvements, V = initial value of property excluding land, and p_n = proportion of total improvements value exempted in year n. For values above \$250,000 under the first option, the rate of return is obtained by averaging the rate for the first \$250,000 with a rate of zero for the amount above the ceiling. If V=0 (the land is vacant immediately prior to the exemption period), any new investment receives the exemption and the rate of return curves follow the dotted lines shown in Figure 2.



a. Option (1) Tax Exemption on Increased Value for Ten Years for all Types of Property



b. Option (2) Sliding Scale of Exemption for Residential Property Only

Figure 2. Incremental Rate of Return as a Function of Investment in Improvements

For the first option, there is no return until the 15% threshold is reached; from there up to the ceiling of \$250,000 the return is a constant rate, and the overall rate declines from there because the portion over the ceiling receives no exemption. If the initial value of improvements is greater than \$1 million, then the curve shown is correct but the applicable portion starts somewhere above the \$250,000 mark on the scale.

With the second option, the highest rate of return is obtained for an investment of 15%, and the rate is the same under both options. Above 18%, the rate of return is equal to 100% of the initial value of improvements; for still higher levels of new investment the rate of return does not change. Lowering the 15% threshold or raising the \$250,000 ceiling would broaden the range of investments that would be eligible for exemption, but would not raise the maximum rate of return. Using a lower discount rate implies a lower rate of return than the curves shown, while for communities with an effective tax rate of 4% (about the highest in Iowa) the maximum rate of return would be a little over 1.5% per year. Naturally, the higher the tax rate the greater the benefit from exemption. Other parameters--the duration of the exemption period, the exemption schedule, and the amount of abatements (currently none)--could also affect the rate of return on investment in improvements.

Duration of the Exemption Period. By increasing the length of the time over which tax exemption is permitted, the present worth of the benefits increases. As an upper boundary, granting the exemption in perpetuity would increase the maximum rate of return up to the effective tax rate (2.5% for the conditions stated in Figure 2); the discount rate chosen then becomes unimportant. A 7-year exemption period combined with a \$50,000 ceiling is shown in Figure 2 for option (1) along with the 10-year exemption up to \$250,000.

Exemption Ceiling. The cutoff above which exemption is not granted has no effect on the rate of return up to the ceiling; for levels above the ceiling, the rate of return declines. The main

purpose of a ceiling is to emphasize small investments (generally residential rehabilitation) rather than large (industrial or commercial redevelopment). A "neighborhood" orientation would be maintained by a ceiling of \$50,000.

Exemption Schedule. As long as the floor remains on the abatement schedule, increasing the percentage of exemption will only serve to bring the rate of return under option (2) up to the rate found in option (1). For the most part, the first option appears to be more attractive than the second.⁴⁵

Tax Abatement. The schedule associated with option (2) is an abatement schedule, in that it applies to the entire value of the property (excluding land) rather than just to the improvements. With the floor (assessed value cannot be reduced below the initial value), the schedule cannot function as an abatement measure, but if the floor were removed or lowered, the second option would become an abatement incentive. Parameters could be adjusted to achieve any particular rate of return desired for any particular level of investment.

2. Revenue Bonds

Iowa currently permits cities to issue revenue bonds for private industrial facilities, and the proposed legislation would extend that authority to all land uses in a designated revitalization area. Cities can obtain credit for private borrowers at a rate about 2% lower than these borrowers could obtain directly; no municipal assets or tax base are pledged to repayment of the bonds, and the borrower pays off the bond as if it were a long-term loan.

If an investor needs credit in order to undertake a revitalization project and the real interest costs or opportunity costs of funds for investment can be lowered by about two percent-

⁴⁵Option (2) becomes preferable for investments such as more than \$280,000 in a building already worth over \$1.1 million, or more than \$400,000 in a building worth at least \$800,000.

age points, then some investment projects will be undertaken which otherwise would not have been feasible. Concentrating these investments in revitalization areas might have a substantial impact under suitable conditions, but these will depend heavily upon the local context.

Combining low interest credit from revenue bonds with the tax exemption provisions, or combining these with other grant and incentive programs provides an extensive and flexible set of instruments for localities to use in addressing problems of urban revitalization. Once the instruments are created through state enabling legislation, localities can determine the mix of instruments to use for particular problem areas.

DISLOCATION AND CONVERSION

Many examples can be found to show that both public and private redevelopment efforts have had adverse impacts on the owners and particularly the tenants of residential and commercial neighborhoods. In an effort to provide a more equitable balance between the public interest and individual interests regarding urban renewal, the Federal Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970 was passed. This required relocation assistance payments to persons and businesses displaced by urban renewal, in addition to compensation for any other property rights acquired by the public sector. The Iowa legislation proposes to incorporate similar provisions.

The bill also includes restrictions on rezoning, both prior to designation as a revitalization area and for five years afterward. The general problem that these sections address is the same, but it can be broken into two components: dislocation of tenants and land use conversion.

1. Dislocation

Although urban "gentrification"--the movement of middle class people into older blighted urban areas, and the attendant increase in rehabilitation and property values--has been

relatively modest in absolute numbers, it has received a good deal of attention because speculation and property value increases have meant that previous low income renters could no longer afford the dwellings they inhabited, or they were dislocated in the process of rehabilitation. This has occurred entirely, or almost entirely, within the context of private market activities.

Relocation Assistance Paid by City. The problem of dislocation is one which exists independently of public programs which may or may not exacerbate it. At the present time, relocation assistance is not provided for persons dislocated by private developers, but is provided for public sector projects. By adding the relocation payment requirements to the Iowa legislation, all private rehabilitation and redevelopment that occurs within an area is brought under the policies that have been previously applied only to public sector development. Relocation assistance will be required for some private investment under revitalization, when that assistance would not have been required without the revitalization designation.

Some of the problems associated with relocation assistance are these:

(1) Relocation costs are hard to estimate before the fact and are often inequitably administered. Under federal guidelines, relocation can cost up to \$4,000 per family in direct payments plus approximately \$300 in administrative services. Iowa City was required to pay relocation, under urban renewal, to students who would have moved anyway.

(2) Dislocation caused by public actions clearly calls for relocation assistance, but the correct policy toward private displacement is less clear. Under revitalization, the line between public and private sector action is blurred.

By being selective in which types of activities (e.g., residential or commercial, rehabilitation or new construction) are eligible for tax exemption and other incentives in a revitalization area, the city can control the amount of displacement

that is likely to take place. Imposing relocation assistance costs on cities will cause them to shy away from areas in which displacement might be a problem, but the flexibility is available to allow cities to tackle revitalization without making themselves liable for big relocation expenditures.

Relocation Assistance Paid by Private Investor. Distinguishing between the issue of the need for relocation assistance and the issue of who pays for it, an alternative on the latter issue is the imposition of costs on the private investor. Definitions of costs and eligibility would be the same, but the private sector would provide the administrative capacity and make the payments. Undoubtedly, some level of public sector oversight would still be necessary.

Private investors are unlikely to engage in projects that will require much in the way of relocation assistance. In particular, rehabilitation of existing residential structures would be feasible only under unusual circumstances. By imposing the costs of displacement on the private sector, a high level of protection is provided against the dislocation of low income residents, but a similarly strong pressure is created to suppress private investment which might have been undertaken had it not been for the revitalization program.

Revitalization Benefits Optional Within Designated Area. To the extent that individual investors within a revitalization area are faced with both the incentives and the costs, the resolution of them could be carried out at the level of the investor rather than at the city level. If, for example, the investor paid relocation assistance and provided relocation services, then any investor applying for tax exemption or revenue bond proceeds would also have to provide relocation assistance. Those not applying for the benefits would not have to comply with the restrictions. The current version of the proposed legislation strongly implies but does not state that all displacement is covered, whether or not caused by investment benefitting from revitalization incentives.

Restriction of Revitalization Benefits to Residential Properties Only. Instead of, or in addition to, the relocation and rezoning provisions, another possibility is to limit the tax exemption and revenue bonding incentives to residential properties, thereby excluding commercial and industrial land uses from some or all of the benefits. If the focus of the legislation is determined to be residential rehabilitation and redevelopment only, then the incentives may, of course, be made available only to that type of land use. The legislature may select one type of use to favor, if it so chooses. Since the incentives would still be available to residential developers to demolish existing structures and replace them with higher density units, the "bulldozing" of people would be only partially affected.

Rezoning Restrictions both Before and After Revitalization. Another approach to the bulldozing problem is to impose rezoning restrictions on revitalization as a condition for receiving the incentives. The current legislation contains such restrictions, but they only apply to conversions from one major use to another and not for shifts within a category; a rezoning from single-family residential to multi-family residential is not restricted. Table 2 shows that dislocation can be prevented by fairly tight and precise restrictions on rezoning, but the same thing can generally be accomplished by imposing requirements for relocation assistance. Since the necessary restrictions on rezoning would rather severely limit the flexibility of local policy makers, relocation assistance would seem to be a better means to the same end.

2. Conversion

If for some reason there is a desire to prevent the character of a neighborhood from being allowed to change, or to prevent the conversion of one land use into another (single-family to multi-family, residential to commercial), then rezoning restrictions as described above can be incorporated into the legislation. Certainly there are individual circumstances that would argue for neighborhood protection and the prevention of

Table 2. Types of Land Use Change and Controls

Existing Zoning	Existing Land Use	New Land Use	Control Measures
low density residential	same	high density residential	rezoning restrictions to include density; relocation assistance
low density residential	high density residential	high density residential	rezoning restrictions to include the requirement that zoning match existing use; relocation assistance
multifamily residential	same	rehabilitation	relocation assistance
residential	same	commercial	relocation assistance; rezoning restrictions
commercial	same	high intensity commercial	relocation assistance for business enterprises; rezoning restrictions to include subdivisions within the commercial category

commercial encroachment, but it is difficult to see why such decisions should be taken at the state level and applied rigidly to all municipalities.

THE LOCAL DECISION PERSPECTIVE

From the fiscal standpoint of the local community, the question is whether the increase in the tax base will offset the short run tax expenditure and other costs. This balance depends upon how much new investment is induced by the revitalization program, relative to the investment that would have taken place in any event (nonaffected investment). It is almost impossible to determine--either a priori or after the fact--what new investment will take place or would have taken place anyway. Provisions which apply to induced investment must also apply to nonaffected investment; there is no practical way to distinguish between them.

Table 3 lists the more evident benefits and costs that would be weighed by a local jurisdiction in determining the feasibility of a revitalization effort. Besides the tax base increase, benefits include general improvements in the quality of life for residents, while the debit side includes various administrative costs plus the loss of taxes on nonaffected investment. These costs and benefits must be estimated individually for each revitalization area in each community.⁴⁶

Assuming that administrative costs can be estimated with adequate reliability, the decision hinges upon whether the revitalization incentives will induce enough new investment to offset the administrative costs and the tax loss on nonaffected investment. Using the provisions of the bill, a tax rate of 2.5% and a discount rate of 7%, the loss on every dollar of nonaffected investment is 18¢ and the gain on every dollar of induced investment is 18¢. This means that for every dollar of

⁴⁶The fact that the list of costs is longer than the list of benefits implies nothing about the desirability of revitalization; it may well be that the sum of all the items in the right column is much smaller than the present value of the tax base increase.

Table 3. Benefits and Costs from the Local Perspective

Benefits	Costs or Disbenefits
long run increase in the tax base	taxes foregone on nonaffected investment additional assessment workload relocation assistance payments and administration administration of exemptions (applications, review, tax bills) rezoning restrictions planning administration of referenda

nonaffected investment that takes place, there must be enough over 50¢ worth of induced investment to cover the administrative costs of the revitalization program. The 50-to-100 ratio depends upon the discount rate chosen but not the effective tax rate of the community. In other words, given the tax exemption provisions in the bill and a 7% discount rate, at least 50% of the investment applying for exemption must be induced investment in order for the community to break even; at a 4% discount rate, the breakeven threshold drops to 32% induced investment.

PROGRAMS OF OTHER STATES

Many states and cities have enacted and implemented property tax exemption and/or abatement programs. A recent study done by The Urban Institute, which surveyed eight cities in forty states, reports a wide range of such programs being used to stimulate housing rehabilitation. Because of the comprehensive and timely nature of this report, it will be extensively examined here. In addition, several specific examples of states neighboring Iowa will be reviewed.

1. Urban Institute Survey⁴⁷

The Urban Institute study is primarily concerned with property tax exemption programs; the report does not provide extensive information concerning the use of Industrial Revenue Bonds, which is the second major tool used in Iowa's pending legislation. The report does, however, provide descriptions of 28 individual cities' programs where property tax exemptions are combined with a wide variety of other revitalization tools.

Concerning property tax exemptions, the study found that of the 40 states surveyed:

** Twenty-three states have property tax exemption enabling legislation. Most of this legislation has been enacted in the past 5 years.

⁴⁷"Comparison and Summary of Property Tax Relief Programs for Housing Rehabilitation," George A. Reigeluth, et al., The Urban Institute, September 29, 1978, 124 pages.

** Local property assessment practices must be considered in evaluating the probable success of tax exemption programs. Involvement of owner-developers depends to a great extent on their perceptions of the assessment procedures of a particular city. Owners may fear, for example, that by reporting improvements they would be calling attention to an apparent underassessment (assessed values are frequently below their legally mandated levels). Nineteen cities in 9 states (including Nebraska, Ohio and Wisconsin) have "de facto" property tax exemption programs (mostly for routine maintenance and repairs). Nine of these cities are in states that have exemption enabling legislation. Here, there is no formal city legislation, but the assessor does not increase assessments for certain improvements. Whatever the situation, it would appear important to have a well defined formal property tax exemption policy which is uniformly enforced so that property owners will know what to expect.

** Twenty-eight cities in the survey had active property tax exemption programs.

** Three cities also have property tax abatement programs where part of the cost of the improvement is actually deducted from the pre-improvement tax base.

Comparison of the 28 "Active Cities" Programs

** Fifteen cities (slightly more than 50%) exempted 100% of the value of improvements from assessments for 3 to 7 years.

** Three cities have no predetermined exemption terms. Instead they work out individual contracts with property owners.

** Among the remaining cities surveyed, there is a wide range of exemption practices. (Boston exempts 100% for the life of the improvement in certain cases.)

** The "effective tax rate" of these cities ranges from .65 to 6.2 percent. Of course, exemption programs tend to be most effective where the tax rate is high.

** Most of the 28 cities "target" their programs according to:

- 1) eligible rehabilitation work -- maintenance and improvement only; conversion to multi-family only; up to \$10,000 per unit only; more than \$2,500 or \$5,000 per unit only.

- 2) eligible structures -- one or two family dwellings only; multi-family dwellings only; dwellings more than 20-30 years old; low value buildings (the worst housing).
- 3) eligible persons -- Four cities give preference to low to moderate income owner-occupants.
- 4) geographic location -- Eight cities allow exemptions only in designated (blighted) areas.

Participation. Data are somewhat incomplete, but in 16 cities where data are available, fewer than 1% of the total eligible applicants participate in exemption programs.

- ** Of the three cities with participation rates greater than 1%, two have very deep exemption/abatement subsidies and one supplements the exemption with other subsidy-type programs.
- ** Where information exists (10 cities), the characteristics of participants vary greatly. Some cities have mostly middle to upper income participants, others have a preponderance of absentee investors, and in two cities the participants are mostly low to moderate income owner-occupants.
- ** Factors which affect participation include program design, extent of the exemption subsidy, housing market conditions, local property tax system, and the nature and extent of other related revitalization programs operating in the area.

A subsequent paper, which may be completed in the near future, will attempt to explain and analyze the effectiveness of specific programs.

2. Other Programs and Proposals

Several specific examples may be of assistance in demonstrating the range of tax exemption/abatement and other programs being used in other states.

- ** Legislation which was recently summarized in Urban Land⁴⁸ indicates that "In Missouri, the 1949 State Urban Redevelopment Corporation Law enables cities

⁴⁸Cheryl Baxter, "Economic Development and City Revitalization," in Urban Land, Vol. 37, No. 8, September 1978, p. 16.

over 350,000 to create redevelopment corporations empowered to grant a 25-year tax abatement in blighted areas. Improvements are not taxed during the first 10-year period.... Taxes during the next 15 years are based on a 50 percent valuation of the developed property."

- ** Indiana allows no increased property taxes on assessed value of improvements during the first year and gradually increases to 100% in five years.
- ** In Michigan, legislation has recently been enacted which permits exemption of property taxes for the restoration, replacement or construction of commercial facilities in special zones.⁴⁹

Finally, a number of recommendations have been made which would supplement property tax exemptions. A good summary of such recommendations is found in a recent study done by the California Public Policy Center.⁵⁰ This study suggests that the variety of policy instruments available should be combined in such a manner as to coordinate the resources of all the "principal actors... owners, tenants, financial institutions and governmental agencies" who must work together and foster "a basic desire on the part of the community to sustain itself."

⁴⁹ Community Planning Report, Vol. IV, No. 35, October 2, 1978, p. 334.

⁵⁰ Saving Neighborhoods, Programs for Housing Rehabilitation and Neighborhood Revitalization, Cary D. Lowe, California Public Policy Center, March 1978.

COUNTERINCENTIVES TO URBAN REVITALIZATION

For several decades there have been suggestions that suburbanization and sprawl have been at least encouraged by government policies, if not primarily stimulated by them.⁵¹ In regard to revitalization, the argument is that less revitalization takes place because the investment that might have occurred in urban areas is redirected toward the fringes of urban areas. Thus one major policy strategy for encouraging urban revitalization would be the correction of existing policies that are biased toward sprawl.

To the extent that such biases can be found, they are generally the result of side effects from programs designed for other purposes. Low interest mortgages for the purchase of single-family homes, highways that improve access and goods movement, sewage treatment facilities that improve water quality, and tax policies that protect family farming may all create systematic incentives for rural fringe development at the expense of urban areas. Although the existence of unintended side effects is plausible, there has not been enough research on the impacts of most of these policies to be able to evaluate how strong the effects are. The possible incentives to sprawl listed below are developed to the point of being reasonable hypotheses, but they are not necessarily established relationships.

Based on the survey undertaken for this report, most of the programs that appear to encourage sprawl originate at the federal level or at the local level. To the extent that there are inconsistent policies, they are between different levels of government or within levels other than the state level. The list is by no means exhaustive, and it is offered in the hope that it will lead to further thought.

1. Highway Subsidies

Viewed as a public service, streets and highways are for the use of everyone and everyone benefits from them, either directly

⁵¹A recent group of examples can be found in the Journal of the American Institute of Planners, 41, 6 (November 1975).

or indirectly. Unfortunately, this view is misleading, because the benefits of travel are almost entirely captured by the user, and failing to make the user pay the full cost creates an incentive to overuse the service. Roughly a third of the road mileage in Iowa sees fewer than twenty vehicles per day, and almost all of this mileage is in rural areas. Yet they are sprinkled with non-farm residences, whose occupants commute to some urban area, while the roads are maintained largely at taxpayer expense. Roughly 60% of the expenditures on county roads comes from property taxes, paid in part by agricultural landowners.⁵²

Expenditures tell only part of the story. If a private enterprise were operating the highway system, it would have to pay property and sales taxes and earn a reasonable rate of return on the land used for transportation purposes. Measured against this criterion, highway users pay only about 10% of the full social costs of the facilities. Thus all highways are heavily subsidized from the user's point of view, and the result is that residences, workplaces, and shopping areas are considerably farther apart than they would be if the highway user were charged for the full costs of the service. Most of this subsidy is granted at the local level, although there are state and federal policies which tend to limit the amount of discretion localities have in correcting this inefficiency.

2. Housing Finance

Direct grants for single-family housing, low-interest mortgages such as FHA loans, the deductibility of interest payments for income tax purposes, and the preference of private lenders for new suburban development versus older urban neighborhoods have all contributed greatly to the tendency for urban areas to spread out. Each of these policies contains a bias toward greater consumption of land, especially suburban and fringe land.

⁵²Douglass Lee and Steven Kautz, "Highway Financing in the State of Iowa," Technical Report 84 (Iowa City: Institute of Urban and Regional Research, The University of Iowa) March 1977.

3. Sewerage and Sewage Treatment Facilities

In the name of pollution control, EPA has provided grants of 80% of the costs of new treatment and collection facilities to localities across the country. While the goals are laudible, the subsidy mechanism for achieving them creates a distortion in the pricing of collection and treatment that again lets the fringe dweller avoid most of the real cost. As with highways, the benefits are captured primarily by the user, and the environmental objectives could better be accomplished by development standards and effluent charges. Urban taxpayers--nationally as well as locally--are paying for these extensions. EPA did not start this trend, since localities have long been charging new hookups at average rather than incremental cost, but the EPA program came along at just about the time that growing areas were beginning to correct their pricing policies.

4. Tax Base Inequities

There was a time when dynamic cities had sufficient wealth to tax that siphoning off some of that tax revenue to give to rural areas did not seriously affect the economic health of the cities. Nowadays, the suburbs are generally the jurisdictions where wealth is manifest, and older urban areas cannot tap this source of revenue. Even in small urban areas, growth takes place in low tax areas outside incorporated municipalities, while the residents of these fringe areas still rely upon the sources of employment, income, and culture available in the urban areas.

For public services that generate benefits for a large community, the tax base used to pay for those services should be approximately consonant with the service area. In general, if a person can still enjoy the benefits of services provided in an urban area, he or she should also contribute toward paying the costs. If the service primarily benefits the persons consuming it (e.g., highways and sewers), then the costs should be reflected in the price of the service; if the service creates general benefits (e.g., education, general government), the beneficiaries should be included in the appropriate tax base. Tax base sharing

is one way for the artificial barriers of fragmented municipal incorporations to be overcome; annexation is another way.

The effect is exacerbated by the preponderance of tax-exempt property located in the center of urban areas. To the extent that churches, schools and other public and semi-public activities serve an area that is larger than the tax jurisdiction in which they are located, residents of that jurisdiction are forced to make up the missing tax revenues. The tax burden can be escaped while still enjoying the services by moving outside the jurisdiction.

5. School Busing

Primary and secondary education creates general benefits for everyone in a community, whether they have children or not, and a general tax base (property or income) is a suitable instrument for financing this education. To some extent, it is necessary to adjust funding formulas to take into account special cost problems that some urban districts may have, but the state and local mechanisms are mostly available for this. Transportation, however, is a separable component, and it may be necessary somehow to incorporate these costs into the tax structure. As things stand at present, the per-pupil cost of transportation is much higher for rural residents of a school district, while urban property taxpayers end up paying the bill.

6. Utility Extensions

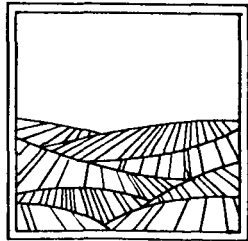
Similar to highways and sewers, water and power services are generally provided to rural residents at a cost that does not reflect the value of the facilities that they alone occasion. Although these utilities are more or less self-supporting (in contrast to highways and sewers), the cross subsidy from easily served (urban) customers to less easily served (rural) customers is still an inefficiency that encourages more dispersal than would be socially optimal.

7. Agricultural Tax Preference

Taxing agricultural land on a basis that is lower than what urban land users pay may improve equity in the distribution of the tax burden and may help to protect prime agricultural land in some cases, but it also allows real estate developers to speculate in fringe or even urban land without bearing the full cost, while forcing development to spread out to more distant sites. Ideally, the cost of developing agricultural land that is removed some distance from an urban area should be prohibitive because of the cost of extending necessary urban services, while the cost of keeping developable urban land in agriculture would be high because of the value of the land for other uses. Existing tax policies tend to distort this pattern of land prices and taxes.

This list of potential or real incentives toward sprawl is only a beginning, and a good deal of hard theoretical and empirical analysis is needed before strong conclusions can be drawn about their effects on urban development and revitalization. Even if some of the effects are minor, however, the extensiveness of the list strongly suggests that a host of programs and policies are systematically pushing investment away from urban areas and into the fringes. Any revitalization program must struggle uphill against the counterpressures of subsidized sprawl, and the fastest route toward revitalization may be to remove the counterpressures as well as to build up new programs to offset them. The benefits of existing programs to rural and agricultural areas can be retained while eliminating the incentives that cause urban areas to spill out onto good agricultural land.

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