Effects of System Development Charges on the Amount of Development

TSDC Update Project

The City of Portland Department of Transportation is currently in the process of reviewing and updating its TSDC methodology and charges. The update project includes this summary of research about the effect of SDCs on development, such as the relationship between the amount of fees and the number or value of permits issued. This report includes synopses of recent major research that study these relationships, a review of the very limited literature about transit oriented SDCs, some practical observations about SDCs, and a bibliography of other studies that pertain to SDCs (also known as impact fees). The report is organized as follows:

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Pages 5-7: Summary of Research about Transit Oriented SDCs

Pages 7: Practical Observations about SDCs

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Summary of Research about SDCs (Impact Fees)

We selected four studies conducted since 2002 that are representative of the research on the relationship between SDCs (impact fees) and the amount and pace of development. They are presented in chronological order:

"An Empirical Investigation of the Effects of Impact Fees on Housing and Land Markets"

Keith R. Ihlanfeldt and Timothy M. Shaughnessy. 2002

The paper evaluates studies of the effects impact fees have had on the price of new and existing single-family dwelling units as well as undeveloped residential land, and presents research of these relationships in Dade County, Florida.

The paper divides the theoretical literature on the incidence of impact fees in existence at the time of the report (2002) into two categories:

1. The "old view" that treats impact fees as a one time excise tax: a fee that increases the cost of housing and hence results in a lower net developer profit resulting in a lower quantity of housing built while ignoring the new infrastructure that the impact fees provide; (Altshuler and Gomez-Ibanez 1993; Huffman, et al. 1988; Singell and Lillydah;, 1990) and

2. A "new view" that brings the public facilities that the impact fees fund into the picture, acknowledging the effect impact fees have on property tax rates and the capitalization of the infrastructure financed through impact fees on the price of new homes.

The study concludes that impact fees increase the cost of new housing and existing housing at the same rate. The study goes on to state that impact fees do not have a direct effect on the price of housing but it is the benefits that the impact fees provide through infrastructure improvements/expansions that are capitalized into the price of new and existing homes. These infrastructure improvements are viewed as benefits rather than a cost burden. In addition, new development contributes to the tax base and the local government is able to collect more revenue at the same tax rate. As impact fee revenue is added to the revenue stream the net result is a lower tax rate for existing residents as well as new development (or the tax rates do not increase as new development makes demands for public facilities and services). The study states, "Impact fees are not borne by developers, but rather are willingly paid for by consumers because of improved amenities or lower taxes."

The study also concludes that "...undeveloped land values decline if the increase in the price of housing is insufficient to guarantee developers of new housing a competitive rate of return." Contrary to other studies, this study makes the observation that developers may be unwilling to pay anything other than lower costs for land due to uncertainties about whether or not impact fees (and other development fees) will increase in the future when it is time to develop the previously acquired land.

"Paying For Prosperity: Impact Fees And Job Growth"

Arthur C. Nelson and Mitch Moody. 2003

The paper has two purposes: (1) provide a review of academic literature on the effects of impact fees and the economy in general and (2) to present an analysis of the relationship between impact fees and the economy as defined by job creation. The analysis is based on an assessment of impact fee and economic data for all 67 Florida counties for the time period 1993 to 1999.

Literature Review Summary:

1. Economical Efficiency and Impact Fees:

"When impact fees are equivalent to market prices they are considered to be efficient." (Altshuler and Gomez-Ibanez 1993) "A key advantage of impact fees (and user charges generally) is the possibility of improving economic efficiency in the provision of infrastructure. Resources are allocated efficiently when prices are equal to the marginal cost of a good—the price to produce one or more of something." (Downing and Frank 1983)

2. Impact Fee Effect on Land Supply:

"From an economic development perspective, the availability of key infrastructure such as water, sewer, drainage and roads to land to make it buildable is perhaps the important ingredient to increasing the supply of land commensurate with development pressures." (Blair and Premus 1987)

3. Impact Fees Reduce Risk and Uncertainty:

The results of studies in both Sarasota, Florida and Loveland, Colorado demonstrate that impact fees appear to reduce the uncertainty and risk of development through the funding and implementation of planned capital improvements and the local government's use of impact fee revenue to leverage other revenues to expand public facilities. (Nelson and others 1991, 1992).

Study Results:

The analysis found that impact fees had no detectible adverse effects on job growth and in fact, impact fees seemed to facilitate job growth. The results of the analysis show that there is a significant positive correlation between impact fees collected per building permit in one year and job growth over the next two years. This result refutes an argument that impact fees are a "drag on growth". The conservative statement of the analysis results would be to say that no noticeable adverse effects of impact fees on the economy (as defined as job growth) could be identified. At the opposite end of the spectrum the analysis results could be interpreted as saying that impact fees typically result in economic growth (at least in Florida in the 1990s).

The paper concludes with the caveat that the study results "should not be misconstrued to mean that increasing impact fees will always result in job growth." This result may not happen in areas experiencing declining growth or that already have sufficient infrastructure to provide for growth. However for those areas that are experiencing growth and the demand for additional infrastructure, impact fees can enhance job growth by allowing for the increase in the buildable land supply, even going so far as being necessary to allow growth if the community does not have any other means to expand infrastructure to an acceptable level of service.

"Impact Fees and Housing Affordability"

Vicki Been. 2004

The report evaluates several studies that have been conducted over the last 25 years on the subject of impact fees as a means of growth control and their effect on the affordability and opportunities for housing.

The conclusion of the report states that existing literature doesn't yet establish that impact fees raise the net cost of housing, meaning the price of a residential unit after accounting for the benefits of impact fees such as the amenities that the revenue from the fees provides and savings on alternative financing mechanisms.

Numerous studies were sited in the report that demonstrate that, with all other things being equal, a jurisdiction that uses impact fees presents a lower risk of higher taxes in the future while providing certainty that the quality of life as it relates to the level of service the impact fees fund through infrastructure will be maintained or even improved. This lower risk along with the package of amenities that the impact fees finance makes for a more desirable market in which to buy and sell. As long as residents perceive that the infrastructure (amenities) funded by the impact fee and/or the avoidance of an increase in the tax rates is worth the cost of the impact fees, the impact fees are considered of value to the consumers.

If a community cannot accurately predict how much growth it will have, where the growth will be located and what the impacts of the growth will be, "the resulting uncertainty about future tax levels and service quality will force housing prices down, relative to housing prices in a jurisdiction that offers less uncertainty" (Gyourko (1991); Turnball (2003)). Residents may try to minimize the uncertainty by controlling growth.

If impact fees accurately reflect costs attributable to growth, the fees can enable growth by providing more certainty to existing homeowners to be less reluctant to allow growth because the impact fees reassure existing homeowners that they will not bear the downside risk of whether growth pays its own way.

"Impact Fees and Single-Family Home Construction"

Gregory Burge and Keith Ihlanfeldt. 2005

This study presents a theoretical model that addresses the concern that impact fees are a tax on residential development which reduces the construction of new homes, especially within the small home market. The study encompasses 41 counties in the State of Florida over the time period from 1993-2003. The study makes a distinction between impact fees that fund public facilities that are normally supported with property taxes versus public facilities that are normally supported with user fees (i.e., water and sewer fees). Of the 67 Florida counties, 41 had enacted either impact fees or water/sewer fees or both types of fees over the eleven year time period 1993-2003.

The study findings show that impact fees may reduce housing supply by increasing developer's costs, or they may increase supply by indirectly reducing the developer's project development costs as well as easing up the development approval restrictions relating to lack of public services (i.e., the impact fees fund those public services which are needed to allow growth). Impact fees provide a direct monetary benefit to the community through the development approval process. Opposition to development by the community may be lessened if it is understood that the impact fees will mitigate the additional demand for services that the proposed development will require.

The results of the models used in the study indicate that

- 1. More housing construction occurred if the impact fees are for public facilities that would otherwise have been paid for by property taxes rather than by user fees; and
- 2. Impact fees that fund public facilities that are traditionally supported with a property tax increased construction of all size of homes within inner-suburban areas and medium to large-sized homes within the outer suburban areas. Impact fees that reduce existing development's burden of the cost of public facilities needed for new development allow the construction of more affordable housing in suburban areas.

The study also included an estimate of the some simple housing price models to test the hypothesis of whether or not consumers will find communities more attractive after the adoption of impact fees or an increase in the impact fee rates because of the consumers expectation of an improved level of service per tax dollar paid. The findings support the idea that demand for housing increases in response to either adoption of an increase in rates of impact fees that support public facilities that are typically supported with property tax dollars because of the expectation of future tax savings. Changes in water/sewer rates had a much less significant impact on the demand for housing.

In summary, the study the results show that, while impact fees directly increase developer's costs (and hence the cost of housing or a reduction in the supply of housing if the increased cost cannot be recovered),

- 1. Impact fees may increase the housing supply by indirectly reducing a developer's project approval costs;
- 2. Impact fees may increase the housing supply by enabling more proposed developments to be approved; and
- 3. Impact fees may increase the demand for housing as homebuyers realize the potential for a reduction in future property tax liabilities.

Summary of Research about Transit Oriented SDCs (Impact Fees)

In *Impact Fees and Housing Affordability*, summarized above, Vicki Been states, "Various growth management techniques such as impact fees can be perceived by home owners as increasing the value of housing through the public facilities (i.e., amenities) that the fees support rather than only increasing the cost of housing. This increase does not necessarily make the housing unaffordable if the amenity received is of value to the consumer. For example, if access to public transportation is an amenity of impact fees the additional housing cost may be offset by a decrease in a family's transportation costs."

There are very few SDCs (impact fees) that include public transportation, therefore there is not much research that has been conducted about this subject. Furthermore, we were unable to find

any other jurisdiction that discounts or exempts impact fees for transit oriented development. The following are summaries of two impact fee studies in California that include transit.

San Francisco, California Transit Impact Fees:

TCRP Report 31 Funding Strategies for Public Transportation, Volume 2 Casebook, Transportation Research Board, National Research Council, 1998...Transit Impact Fee San Francisco Municipal Railway, San Francisco, California

SFGOV San Francisco Chapter 38: Transit Impact Development Fee (http://www.municode.com/content/4201/1413/HTML/ch038.html)

The City of San Francisco has enacted a transit impact fee to cover the cost of providing transit services. The transit impact fee rate study is a stand alone study and is not a component of a traffic or multi-mode transportation impact fee. The original assessment area was the downtown area but this was expanded in 2001 as development spread outside of the original assessment area. The initial fee was assessed only to office space with the assumption that other uses that compliment office buildings (retail, restaurants and other attractions) would result in minimal transit use. The intent was to encourage mixed use development (residential, retail, and office mix) which would require less travel and therefore less demand on the entire transportation system.

An update of the transit impact fees was done in 2001 and the results showed that additional types of development were putting a strain on the transit system and that development was moving outside of the original assessment district so the rates were expanded to include other non-residential types of development and the assessment district was enlarged.

The impact fees cover only transit costs, and not any other mode of travel. The fees are calculated from a base service standard which is the ratio of the revenue service hours (i.e., the number of hours that the Municipal Railway (MUNI) provides service to the public on its entire fleet of vehicles [buses, cable cars, light rail]) and the estimated number of auto and transit trips (trips exclude pedestrian and bicycle trips). According to the study update (Nelson/Nygaard Associates, 2001) "an increase in trips resulting from new non-residential development will reduce the ratio of revenue service hours to overall trips generated by new development" In order to maintain the level of service (as measured by revenue service hours per 1,000 trips) the revenue service hours must be increased.

There is no association of the transit impact fee to road impact fees other than the observation that as new development uses private transportation, the resulting increase in private automobile trips will increase the cost of maintaining the base service standard (revenue service hours per 1,000 trips) because the increase in traffic congestion will impact MUNI's ability to maintain schedules

San Jose, California Traffic Impact Fee With Public Transportation Component

Draft North San Jose Traffic Impact Fee Plan, prepared by Hexagon Transportation Consultants, Inc. June 2005

In contrast to the San Francisco Transit Impact Fee, the North San Jose fee is a "traffic" impact fee encompassing roads, public transportation and non-motorized transportation. Also in contrast to San Francisco, the fee applies to residential and industrial development but excludes retail/commercial development. The fee rate is based on an allocation of trips generated via private vehicle, public transportation and pedestrian/bicycle. The rates are based on a distribution of estimated daily trips including a determination of the mode of choice for the trips (i.e., pedestrian, bicycle, transit or automobile). The determination of the mode of choice is 75% auto; 8% transit and 17% pedestrian/bike). The total cost of all needed improvements (road, transit, pedestrian and bicycle) is divided by the net vehicle trips (75% of new trips) which is used to calculate the impact fee rate per unit or per 1,000 square feet for types of development based on their trip generating characteristics.

Practical Observations about SDCs (Impact Fees)

The primary focus of the academic literature about impact fees is to evaluate and explain the effects of impact fees using economic tools, models, concepts and vocabulary. In addition to these important and powerful analyses, it is possible to view impact fees through the lens of common sense. The following are practical observations about impact fees:

- 1. Impact fees are charged in places that are growing, because the fees are charged only to the growth. If there was no growth, there would be no revenue from the impact fees.
- 2. Hundreds of local governments in at least 33 states charge impact fees and collect significant amounts of revenue from those fees.
- 3. Impact fees in those growing communities have not stopped development. If the fees stopped development, there would be no impact fee revenue collected by the local governments.
- 4. It is probably impossible to determine whether or not there would have been even more development if those communities had not charged impact fees. What is known is that growing communities with impact fees continued to experience growth, and the impact fees helped pay at least a portion of the infrastructure needed for that growth.
- 5. Impact fee revenue provides hundreds of millions of dollars for infrastructure needed by development.

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