INTERNATIONAL CONFERENCE ON MUNICIPAL FISCAL HEALTH

WORKSHOP: LAND AND URBAN DEVELOPMENT

11:15 AM – 12:15 PM, MAY 23, 2018

LINCOLN INSTITUTE OF LAND POLICY

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Two ways to improve revenue with no deadweight losses

- Municipalities around the world are struggling to pay for their services.
- It is possible to reduce costs specially using the advances in technology.
- The room for increasing revenues is limited but not impossible. The answers are in Land.
- I will focus on two actual strategies to improve revenue that do not distort the economy but rather correct for negative externalities.

Charging for the right of construction

- Economists claim that a charge on land will not distort the economy since its supply is totally inelastic.
  - When a developer increases the FAR, it is "creating land".
- It is not indubitable that created land would be totally inelastic but it is at least reasonable to assume so.
  - In a specific area of the city, it is probably very hard to increase final prices; perfect competition among developers will transfer all the charges to land.

Format 1: defining a value ex-ante

- The simplest way to charge for building rights is defining a fee per square meter.
  - It is called “Outorga Onerosa do Direito de Construir” (OODC) that means “Onerous Rights of Preemption”.
- The fee ideally would capture the impact on land value implicit in increasing the FAR.
- Assuming that the land price/square meter at FAR = 1 **and** the (final) housing price/square meter is knew, it might be simple to evaluate the gains from increasing the FAR but:
  - It is difficult to evaluate how people value low density.
  - Estimating the final price is far from straightforward since it is usually a new development.
- Currently there is a blood in São Paulo regarding the value.

Format 2: Auction

- A perimeter and a schedule of investments are defined for redevelopment called “Urban Operation”.
- A bond is created (called CEPAC) corresponding typically to the right to build 1 square meter.
  - Some adjustments are made so one square meter might need more or less than 1 CEPAC.
  - In some cases it is possible to use CEPACs to convert 1 square meter zoned as residential to commercial.
- All bonds are auctioned in the stock exchange market (Bovespa).
  - There is no secondary market.

Comparing the systems

- The logic of both instruments is the same.
- There has never been disputes over CEPAC value since it was defined by the market.
- CEPAC revenue seems larger than the revenue from OODC but it is more uniform.
  - Each Urban Operation is capturing from USD300 millions up to USD800 millions. OODC revenue is around USD50 millions per year.
- CEPAC represents a significant amount for the City and it is able to finance a large portion of the public investment in the redevelopment.
- OODC revenue is not so large (compared to total revenues for São Paulo) but it is quite relevant for funding small and medium urban interventions.

Regulating Transportation Network Companies

- A fixed amount per mile with passenger
  - More expansive in peak hours in the center
  - Less expansive in the periphery, off hours, weekends…
  - Less expansive for women drivers, non-fossil vehicles, accessible vehicles, pool…
- There is no auction since the amount of miles is not fixed ex-ante
  - 5,000 “taxi-equivalent” (incremented to 10,000) target to be reached using the pricing system.
- TNCs must open their data but…
  - Taming Uber is not so easy (the step not taken)

Why (not) charge for the use of roads?

- Around 25% of the land in any city is dedicated to the road system.
- It is by far the largest share of public land.
- Most cities charge for any urban land but the urban land dedicated to roads.
- If you include the charge in the property tax, users and non users of the roads will be paying the same.

Vickrey Taxation

- Every road should receive at least the proportional maintenance cost from its users (benefit tax).
- Congested hours/sites should pay for the negative externality using the road generates on all other users (Pigou's corrective tax).
- It is possible to separate the two components (space and time) to create a "more than optimal" taxation.

Revenue Potential

- Currently: US$50 millions per year
- Property tax in São Paulo: US$2 billions per year
- Increase in use expected to be around 10 times in 5 years; 25 times in 10 years.
- We could charge all commercial use of urban roads: trucks, service providers, armored cars…

Stock and Flow

- Property tax: charge a flow based on a stock (the property)
- Value capture: charge a stock (lump sum) based on a flow (future price appreciation)
- TNCs pricing: charge a flow on a flow; there is no *a priori* stock of miles (no auction, consequently)
- It is a charge on the commercial use of a public land (the roads)
  - Without value capture, developers would make a private gain given a public investment. The same logic applies.

The Future of Land Taxation

- Traditional land taxation is virtuous: it does not generate deadweight losses.
- The fee on TNCs is one step ahead: it also corrects a negative externality.
- Airbnb offers more rooms than the largest hotel chain in the world (Intercontinental).
- Are we going to change the way we tax land? What if we charge differently for over and under density?

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