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THE REVENUE UNDER OUR FEET: LAND RENTS RESOURCES & TAX POLICY



Flexibility in the CLT model:

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Edward Dodson*

Scattered-Site Properties and Community Land Trusts:

A Strategy for Expanding the Supply of Permanently Affordable Housing

Edward Dodson M.L.A.

The declining affordability of decent housing is a problem all across the United States and beyond. For many low- and moderate-income households, the prospects for homeownership have almost disappeared unless public subsidies are provided to developers, and the terms of mortgage financing allow for minimum borrower cash contributions to the transaction and flexibility regarding income, employment and creditworthiness criteria. While these measures historically carry a higher risk of borrower default, the worst-case scenarios are most often triggered by economic downturns and rising unemployment.

Affordable housing is again an issue of national importance; after a half-century of increasing owner-occupancy, that increase of owner-occupiers has stalled, even as the supply of affordable rental options has declined.

This reduced access to affordable housing is again a serious societal problem, with widespread economic consequences. The depth of the problem is succinctly described in the 2016 State of the Nation's Housing report by the Joint Center for Housing Studies of Harvard University:

On the renter side, the number of cost-burdened households rose by 3.6 million from 2008 to 2014, to 21.3 million. Even more troubling, the number with severe burdens (paying more than 50 percent of income for housing) jumped by 2.1 million to a record 11.4 million. ...In all but a small share of markets, at least half of lowest-income renters suffer from housing cost burdens. While nearly universal in the lowest-income households, cost burdens are rapidly increasing among moderate-income households as well, especially in higher-cost coastal markets.

During the peak of the last property market cycle, the U.S. Congress created the National Housing Trust Fund, charged with assisting those who can least afford the cost of housing under existing market conditions. The first funding under this program was announced in May 2016 (albeit at disappointingly low amounts). It is recognized that public and other subsidies are necessary because of one crucial fact too often ignored or downplayed by economic analysts and policymakers: land markets have been made inherently dysfunctional by very low effective rates of property taxation.

Every parcel of land has some rental value in the marketplace. The difference between this market rental value and the annual revenue collected via the property tax represents an imputed income stream to the landowner. Market forces capitalize this income stream into the price for land. In communities and regions blessed with strong business activity (and, therefore, a sound employment base) poverty may not be visible or reflected in large numbers of homeless people. However, the

demand for housing -- and for sites upon which to construct housing units -- always translates into highly speculative land markets that pull up the cost of building sites to levels where the construction of units affordable to many households is nearly impossible without substantial public subsidy.

In many areas of the nation's cities, the land cost component has now recovered since the 2010 market.

Public policy has thus far primarily relied on a combination of interest-rate subsidization, liberalization of income and creditworthiness requirements and direct grants to mitigate the problem of housing affordability. Local governments have also attempted to make low- and moderate- income housing profitable to developers by approving higher density construction, contributing publicly held land when available.

These approaches have achieved some notable successes; however, argument has ensued over the cost incurred by taxpayers; and, more importantly, that the problem of land price escalation has outpaced these measures.

The community land trust model of ownership offers a potentially self-sustaining vehicle for mitigating the long-term problem of providing affordable housing in the absence of getting local communities to implement the public collection of the potential annual rental value of locations.

Land trusts have a long and positive history in the preservation of open space and as administrative bodies for leasehold residential communities. There are around 250 CLTs scattered around the United States, the largest -- with 2,000 homes -- is in Burlington, Vermont. Starting these communities where the need for affordable housing is most severe requires the acquisition of large tracts of land, a near-impossibility in today's era of high land prices.

Another strategy is needed. A potentially useful approach is to take advantage of existing housing units and bring them into the community land trust under a scattered site strategy. A small number of such programs already exist. In Washington State, for example, the OPAL CLT has brought nine scattered-site properties into the trust land. While such efforts are laudable, the scale of the affordable housing problem requires a program design with the potential to include hundreds or even thousands of properties.

CLTs can make effective use of a scattered-site strategy to remove the cost of purchasing land for the homebuyer, acting as a co-purchaser of existing real estate with matching qualifying homebuyers meeting program requirements established in partnership with lending institutions, state or municipal housing finance agencies and participants in the secondary market for residential mortgage loans.

The trust would take title to the land itself, and the homebuyer would purchase the home. The CLT would then charge the homebuyer an annual ground rent by a predetermined formula. Ideally, the

homebuyer would be charged a yearly ground rent based on what is determined to be affordable, but no higher than the full current market ground rental value of the location.

Example: if the selling price of the real estate is \$200,000 and an independent appraiser values the house at \$120,000 and the land at \$80,000, the homebuyer would obtain permanent mortgage financing based only on the \$120,000 purchase price of the house. The land trust would purchase the underlying land for \$80,000.

The cash required from the homebuyer for the minimum acceptable down payment plus closing costs associated with the transaction would be substantially less than had the homebuyers acquired title to both house and land. The monthly remittance of ground rent to the land trust would be pegged into the homebuyer's ability to qualify for the mortgage financing based on income.

The success of the community land trust as a not-for-profit entity depends on the availability of a revolving fund to facilitate the land purchases. Potential sources of funding include both government agencies and private foundations committed to housing affordability objectives (and, potentially, grants made from the National Housing Trust Fund).

In cities with large amounts of land in a district already acquired by an authority such as a land bank, disbursement of land at a nominal price. This attractive option would not only make the CLT less expensive to launch but would reserve to the CLT economic land rent sufficient to provide revenue from commercial/retail tenants, much as a traditional ground lease allows an investor to rent land while owning any improvements.

Additionally, the land itself could serve as collateral for borrowing from regional financial institutions that might be induced to approve grants to the trust and/or provide below-market rate financing as part of their commitment to community lending.

Supporters of land value taxation could encourage municipalities to consider adopting a general surtax on assessed land values as a mechanism for providing funds to the land trust.

It must be admitted that supporting CLTs with public revenue – or exempting trust land holdings from the local property tax – is counter to the community commonwealth perspective that all owners of land ought to contribute the market ground rent of land to offset the cost of public goods and services.

CLTs do not – cannot – exist outside of the attachment to the larger community. However, unlike older trust community models (Fairhope, Arden), other CLTs do not rely on ground rent revenue to pay the property taxes on individually owned housing units. Thus, the larger population is required to subsidize the cost of public goods and services brought to CLT held land.

The ground rent charged to the homeowner could be paid directly to the trust or indirectly by arrangement with the mortgage servicer as part of the total monthly housing payment.

What is unique about the scattered-site strategy is its potential to become self-sustaining. No restrictions should be imposed on the resale of homes purchased with community land trust assistance.

At the time of resale, the distribution of proceeds between the homeowner and the trust would be apportioned based on a reappraisal of the real estate. Any increase in land value returns to the trust. The value of any improvements added to the structure will be reflected in the appraisal and distributed to the homeowner. Based on the selling homeowner's current income, this household may still be eligible for assistance under the trust's program but is free to look for a new property based on the neighborhood where they now desire to live rather than only in those neighborhoods or communities where a fixed-site trust has homes or contiguous building lots available.

Another direct benefit of the program is that trust involvement would be of no notable or unique influence on the property market; only the parties directly involved in the transaction need be aware that the homebuyers do not own the land. No special zoning or density variances are required by the government, and the properties will be scattered within existing communities rather than concentrated, as is now the case with most subsidized housing.

A region might eventually experience the creation of more trusts, each designed to serve a particular segment of the population (e.g., seniors and physically challenged persons who require specific housing characteristics). Some potential homebuyers might be eligible to secure financial support from different sources (e.g., labor unions, pension funds, religious organizations, corporations, etc.).

Administration of the scattered site program by the land trust can be expected to be much less demanding than most other housing programs because of the partnership with mortgage servicers.

Employers concerned about the expense of transferring individuals into areas with high housing prices would find it very cost effective to contribute to the trust (as a charitable contribution) in lieu of providing repeated relocation grants and other forms of compensation adjustments to employees, to say nothing of the tax benefits of contributing to a not-for-profit organization. This is becoming increasingly important in areas where the cost of housing has driven up wages for workers beyond what employers can pay and remain competitive in the global marketplace.

The scattered site program as described here will not address the problem of housing for those who are the truly poor or live in areas where land values and housing prices are already bottoming. A deteriorated housing stock is, in those instances, closely related to a general absence of employment opportunities even at modest levels of income.

However, with fewer demands on government to subsidize the housing needs of lower-middle-income households, perhaps the government can concentrate its attention on the revitalization of depressed areas and to providing residents of such communities with desperately needed public services. What the scattered site strategy does offer is a promising addition to the inventory of options available to those who are committed to expanding the opportunities for affordable housing to those who have priced out of the market.

Ed Dodson worked in various management and analyst capacities at Fannie Mae from 1984 to 2005, the last decade within the company's Housing & Community Development Group. Out of his ongoing relationships with the growing number of community land trusts being formed, he developed a model to significantly increase the market penetration of CLTs by adopting a scattered-site approach. Ed is pleased to respond to any questions at edod08034@comcast.net.