Is capturing the "unearned increment" in land value still a viable idea? A cross-national analysis

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Abstract*
The financial aspects linked to planning regulatoin impact the built environemnt. The idea that the public should reaping the ―unearned increment" or the ―plus value" of land is by no means new. The underlying rationale is that much of the value of real property is created not by the landowner‘s work, but by government policies that grant development rights or by broad economic and social trends.
Drawing on the author‘s comparative research on the laws and practices in 13 advanced-economy countries around the world, the paper addresses the degree to which recapture of the ―unearned increment" is indeed a useful approach that policymakers should adopt for financing or incentivizing the delivery of public services and affordable housing.
The idea of value capture in its pure form has failed to catch on widely among advanced economies, but the basic idea has not died away. In recent decades, several ―mutations‘ of this idea have been gaining popularity in many countries, but in widely different forms and degrees.
Keywords:
betterment tax, development control, planning law, real-property taxation, value capture

1 Introduction

The built environment is shaped not only by the direct regulatory instruments that planning law provides, but also by the ancillary financial aspects. These deserve more attention. Few issues in land-use planning are as universal as the bipolar relationship between planning regulation and property values. This issue carries deep economic, social, and distributive-justice implications. Do governments have the right to reap some of the increment in value attributable to planning decisions? And the corollary: Do governments have an obligation to compensate private landowners for value decline due to land-use regulations? Two American scholars have whimsically tabbed this issue as ―windfalls" and ―wipeouts" (Hagman and Misczynski 1978). This topic has trailed planning policy for a long time, yet is no closer today to being resolved in a politically or legally sustainable manner.
This paper revisits the upward side of the land-value coin: How relevant is it today around the world, and especially among advanced-economy countries? The idea that landowners should share some of the increased value of their land with society encompasses a wide range of situations and policies. I will first address the issue broadly and then focus on one specific type of value capture—where the rise in property values is due to land-use regulations or public works. This topic has not

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benefited from enough comparative research.[1] By analyzing the experiences of a large sample of advanced-economy countries, this paper seeks to contribute to knowledge sharing on this important issue.

2 The Idea of Land-Value Capture

The idea that the value of land is created by society and should therefore be reaped for the public is by no means new. The brief survey reported here first looks at the evolution of the notion of the “unearned increment” in land in general, and then specifically at the idea of capturing increments created by land-use regulation.

2.1 Henry George and the “Single Tax” Idea

In 1879 the American thinker Henry George famously proposed the “single tax” idea in his book *Progress and Poverty.* He argued that if the rent from land alone (without the buildings and other “improvements”) were to be paid to the government authority on an ongoing basis, it would suffice to finance the entire set of society‘s public needs (Andelson 2000, xxii -xxiv). A tax on land would avoid causing the kind of economic turbulence that taxes on labor and mobile or financial capital inevitably create. This latter view is supported by many economists (Ingram and Hong 2007; England 2007; Netzer 1998). George (1962) argued that public capturing of land values represents “a takings by the community, for the use of the community, of that value which is the creation of the community” (421). At the time, his proposal did not link value capture with land-use regulation because he wrote the book long before these were established in their modern format.
The “Georgian movement” still draws dedicated followers around the world (as well as many critics; see Andelson 2004).[2] (as well as many critics; see Andelson 2004). However, as attractive as the Henry George theory may be, 130 years after he published his seminal book, the “vote” around the world is clear: “no” to the single-tax idea, with a few small local exceptions. Yet the underlying rationale of the Georgian argument is still compelling to many. It is often cited in support of the idea that the added value specifically created by land-use regulation decisions should be shared with the public.

2.2 Value Capture and Land-Use Regulation: The “Betterment Capture” Idea

Historically, Britain led the way in the world discussion about the nexus between planning regulations and property values. The phrases that the British coined for the issue—“betterment and compensation” or “betterment and worsement” (or “worsenment”)—date back to the late nineteenth century (Baumann 1894). In 1909 a British prime minster made the following eloquent statement when introducing a national betterment capture levy as part of the world‘s first national planning act (Housing, Town Planning, Etc. Act 1909 (c. 44)): “It is undoubtedly one of the worst evils of our present system of land that instead of reaping the benefit of the common Endeavour of its citizens a

[1] Despite the ubiquity of the land-value issue, it has not benefited from much systematic comparative research. The only major academic work that looks at both sides of this issue comparatively is the seminal book by Hagman and Misczynski (1977). It surveyed five English-speaking countries (the United States, Canada, Australia, New Zealand, and England) and contributed considerably to the theoretical framing of the issue. Another book, by McCluskey and Franzsen (2005), focuses mostly on developing countries. The “wipeouts” side—called “regulatory takings” in American lingo—has recently benefited from greater comparative attention. My recent book (Alterman 2010) presents an in-depth comparative analysis of the laws and policies of thirteen countries. Alexander‘s 2006 book analyses four countries in depth.

[2] For an example of one of the movement‘s organizations, see http://www.henrygeorgefoundation.org/. See also http://www.earthrights.net/wg/wg1.html.

community has always to pay a heavy penalty to its ground landlords for putting up the value of their land.”[1]

The failure of this British experiment cannot be attributed to lack of enthusiasm. Unlike the United States, Britain has had a long tradition of legislative responses to both sides of the property value effects. Subsequent legislation tried various other formulas, and these ideas were exported to many of the colonies (McAuslan 2003; Home 1997). However, neither side ever worked satisfactorily (Grant 1999), as discussed in section 4.

Since World War II the betterment and compensation sides have been decoupled in Britain. During the height of the war, the British government appointed the Expert Committee on Compensation and Betterment to guide the government in the laws and policies it should adopt for postwar reconstruction. The influential *Uthwatt Committee Report*[2] introduced two important concepts—―shifting value” and ―floating value” (Replogle 1978; Tichelar 2003).

―Shifting value” assumes that the demand for any given type of land use in a particular region is finite. Land-use restrictions in one municipality (or in one part of a city) may cause downward value changes, but at the same time may increase the value of land in another locality where the regulations do permit development. ―Floating value” refers to the speculative nature of potential land values. Landowners tend to assume that if only planning regulations did not stand in their way, a lucrative type of development would ―land” on their own plot of land. However, the notion of shifting value implies that even if land-use regulations were to be abolished, not all landowners would benefit from development (Moore 2005, 3). The assumption that landowners are entitled to compensation for reduction in development rights was thus shaken, while the justification for capturing the added value was reinforced.

Based on this thinking, the UK Town and Country Planning Act of 1947 reformed the entire system. It discarded the idea of ―development rights” granted by plans years in advance and substituted a system whereby each development is approved ―case by case” through a ―planning permission” (Booth 2003). Local government must prepare local plans, but their function is to guide decisions, not to grant development rights. Thus, the very notion of entitlement to compensation was abolished (Purdue 2010). At the same time, the other side of the coin—capturing the betterment value—was fortified. For several decades hence, the United Kingdom seemed to have ―volunteered” to serve as the world‘s laboratory for testing the betterment capture idea, as detailed in section 4.

2.3 Is There Symmetry between Windfalls and Wipeouts?

The UK story brings to mind an obvious question: If landowners are required to share the windfall derived from land-use decisions, should they also have the right to compensation for decrease in property values due to such regulations? And the converse: If landowners are allowed to keep the windfalls, then symmetry of logic would hold that they should absorb the wipeouts and not be eligible to compensation from the public purse.

However, my recent thirteen-country comparative analysis has produced some counterintuitive findings: In most countries, the two sides of the coin are not symmetric either in law or in practice (Alterman 2010, 3–5). The lack of symmetry is usually not even a public or legal issue, except as a teaser by proponents of one side of the debate who wish to highlight the other side‘s ostensibly faulted logic. In all but two among the sample countries (Poland and Israel), the two sides of the land-value coin are currently disassociated. Thus real-life laws and policies do not operate according to the axioms of pure logic.

The following sections take a closer look at specific instruments for value capture, with a particular focus on those directly targeted to capturing value created by land-use regulatory decisions.

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[1] *Hansard* (1909).

[2] The *British Expert Committee on Compensation and Betterment*, Cmd 6386 (1942). This report is known by the name of its chair, as the *Uthwatt Report*. Its importance in shaping British recovery is recognized not only by planners and lawyers but also by historians of British history. See Tichelar (2003).

3 Three Types of Value Capture: Macro, Direct, and Indirect

Despite considerable scholarly literature, *value capture* remains an open-ended term, variously defined and used. Some use the generic term *value capture* to cover any type of policy or legal instruments whose purpose is to tap any form of ―unearned increment," regardless of the cause of the value rise. Others use the same term to denote only the policy instruments targeted at value arising directly from land-use regulation or public works. The most direct term available to denote the latter type of value increase is *betterment*—a word that originated in British English and still has no specific American English counterpart.

There is also considerable vagueness in the literature on whether a policy should be classified as value capture based on its *purpose* or its *outcome*. Some policies not primarily or overtly intended to reap the unearned increment do in fact exact from landowners or developers monetary or money-equivalent contributions. To provide a more level field for research and knowledge exchange, I propose a distinction among three sets of policy instruments that relate to value capture: (1) *macro*, (2) *direct*, and *(3) indirect* instruments.

3.1 Macro Value Capture Embedded in Broader Land Regimes

Macro value capture instruments are not freestanding. They are embedded in some overarching land policy regime, motivated by some broader rationale and ideology. These regimes are assumed to provide a better land and development policy than a market regime. Four major types of land policy regimes have value capture embedded in them—at least in theory. Some authors regard these macro land policies as value capture instruments (e.g., Smolka and Amborski 2007). The four are: 1. Nationalization of all land and direct government control over its use; 2. Substitution of private property by long-term public leaseholds; 3. Land banking; 4. Land readjustment. Because these macro land policies don't feature value capture overtly, they will not be discussed further in this paper.

3.2 Direct Value Capture

Direct instruments for value capture are policies that seek to capture all or some of the value rise in real property under the explicit rationale that it is a legal or moral obligation for landowners to contribute a share of their community-derived wealth to the public pocket. As a wealth redistribution instrument, direct value capture is often regarded as a tax and requires legislative authority. Direct instruments do not need to seek any additional rationales—for example, they do not need to show that the funds are necessary to mitigate negative impacts of the project, or that the properties that generated the funds will also benefit from the services financed by them. The rationale for direct value capture stands in its own right.

Direct value capture may be divided into two subtypes, and the second subtype is further divided into two subtypes:

a. **Capture of the unearned increment:** Where the value rise is not linked to a specific government decision but rather to general economic or community trends.

b. **Capture of betterment**: Where the value rise is due to a specific government decisions is directly caused by specific types of land-use regulatory decisions or by the execution of public infrastructure.

The betterment levy, too, may be further divided into two subtypes. Confusingly, both are often denoted by the same term: *betterment*. I propose to dedicate specific terms for these two types:

- **b1. Development-rights-based betterment:** Where the value rise is due to a planning or development-control decision that applies directly to the land parcel in question and raises its value.
- **b2. Infrastructure-based betterment:** Where the value rise is due to positive externalities from a government decision to approve or execute public infrastructure, parks, or other services.

Capture of the unearned increment type may take many forms, including a capital gains tax on land or real property, an ―unearned increment" tax upon transfer of title, sometimes time-adjusted to curb speculation, or an annual property tax that is closely tuned to the rise in property values. Taxation of the unearned increment is found in several countries. Americans know the examples of Vermont and Pennsylvania (Daniels, Daniels, and Lapping 1986 and by Gihring 1999). In the Far East reported cases are Taiwan (Lam and Tsui 1998), Hong Kong, and Singapore (Hui, Ho, and Ho, 2004) . . .
This paper focuses on the second subtype—capture of betterment arising from government land-use decisions. In sections 4 and 5 I will report on the international experience.

3.3 Indirect Value Capture

The rationale of the indirect instruments differs from the direct ones. The indirect instruments do not seek to capture the added value for its own sake, because it is ―unearned," but in order to generate revenues (or in-kind substitutes) for specific public services. Indirect instruments are usually practiced on the local government level. The objectives behind the indirect tools are usually more pragmatic and less ideological than the objective behind either the macro or the direct capture instruments. To survive legal and political challenge, the indirect instruments usually need the ―cover" of other rationales beyond the desire to capture the unearned increment. It is easy to confuse the indirect instruments with the direct ones because both types harness the same source of wealth—the additional value of real property derived from government land-use and development decisions.
Unlike the direct instruments, indirect value capture is an ever-evolving category of policies that varies greatly among countries and localities. This topic merits its own comparative research. In section 6 I will discuss this topic only to contrast it with direct value capture.

4 Betterment Capture: The International Experience

How prevalent is direct betterment capture around the world? In this section and the following one I report on my international comparative research that focuses on betterment capture practices among advanced-economy countries (with a small detour to South America too).
Many types of government land-use or development decisions could serve as grounds for direct value capture.[1] These vary from country to country and possibly also from one municipality to another. Infrastructure-based betterment levies are historically the earliest form of betterment capture. I will discuss this type first and then proceeding to focus on development-rights-based betterment capture instruments.

4.1 Infrastructure-Based Betterment Capture

The oldest types of the betterment capture instruments are ―infrastructure-based." They focus on value increase to neighboring properties caused by public infrastructure. Public works are a government function that preceded land-use planning laws by centuries. When the British enacted the first town planning act in 1909, they instituted a 50 percent levy on infrastructure-based betterment—an instrument that predated that act. This instrument migrated to many of the British colonies and protectorates but experienced many failures (Peterson 2009, 36–38; Grant 1999; Alterman 1982). Apparently, linking value rise to the execution of public works is not easy. The reasons may include difficulties of proving the causal relationship to the infrastructure works; difficulties in determining the geographic range of impact; and difficulties in levying the charge at a time frame reasonably close to the execution of the public works (because the windfall is usually not realized at that point in time).

[1] In theory, other types of government decisions unrelated to land use could also be the cause of land value increases—for example, a new trade treaty that will influence a border town. However, these have not generated a significant body of law or scholarship and are not discussed here.

Yet this idea resurfaces from time to time. For example, in 2004 the Scottish government commissioned a report on whether betterment could be captured from value increase directly due to new transport facilities. Peterson (2009), writing for the World Bank, and Medda (2010) for the UN report on similar initiatives in both developing countries and advanced economies. These initiatives usually stand alone, unrelated to capture of development-rights-based betterment.

4.2 Development-Rights-Based Betterment Capture

Betterment capture policies may target a variety of land-use planning and development-control decisions. I do not know of any country or locality that has ever implemented value capture instruments to tap all the possible ―stations” along the planning-to-permitting procedures. The international experience shows that only a few of these stations have ever served as grounds for this type of betterment capture.

As part of a large research project on compensation for value decrease (Alterman 2010), I also looked at the value capture side. The sample of countries encompasses fourteen advanced-economy and democratic jurisdictions (thirteen nations and an additional U.S. state). This sample constituted about 40 percent of the thirty-four members of the OECD in 2010. In alphabetical order the sample countries are Australia, Austria, Canada, Finland, France, Germany, Greece, Israel, the Netherlands, Poland, Sweden, the United Kingdom, and the United States (with additional focus on Oregon). The sample was selected to represent a variety of legal and geographic contexts: large and small countries located on four continents; federal and unitary jurisdictions;[1] common-law as well as civil-law countries with varying degrees of constitutional protection of private property;[2] countries belonging to the EU and those outside it; different cultural and language backgrounds, and so forth.

A finding that may surprise many is that most of the sample countries do not practice *direct* betterment capture today. There are only three countries in this sample with significant experience in direct betterment capture instruments: the United Kingdom in the past, and Israel and Poland currently. These countries applied a variety of capture policies, so cumulatively their experiences contain a wealth of potential lessons from which other countries may learn.

4.3 Britain: The World’s Former “Laboratory” of Betterment-Capture Instruments

Britain‘s vicissitudes with various types of betterment capture policies make it the world‘s most distinctive laboratory. Between 1909 and the early 1980s, Britain exhibited pendulum-like shifts in policies about compensation and betterment as power changed hands between Labor and the Conservatives (Tories; Cox 2002; Tiechelar 2003; Lichfield and Darin-Drabkin 1980, 144–145). These shifts were accompanied by ideological debates and significant public exposure.

The various policies adopted and repealed represent a large range of rates of recoupment: the 1909 Housing, Town Planning, Etc. Act and its successors imposed a 50 percent levy on betterment arising from the approval of a land-use plan (called ―scheme” and functioning similarly to zoning). The British exported this instrument too to many of their colonies around the world. It too proved to be almost inoperable due to difficulties in exacting the levy from landowners at the time of approval of the scheme (Peterson 2009, 36–38; Grant 1999; Alterman 1982).

After World War II and the rethinking brought about by the Uthwatt Commission, Labor enacted the 1947 Town and Country Planning Act that imposed a 100 percent ―development charge” on the full extent of betterment. The revenue was to go to central government (Grant 1999; Lichfield and Darin-Drabkin 1980, 136–142). The tax was ineffective (Williams and Hallett 1988, 119), but scholars remain divided about whether it might have succeeded with time (Lichfield and Darin-Drabkin 1980, 142–144). In 1953 the Tories abolished the act.

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[1] The United States, Canada, Australia, Germany, and Austria are federal jurisdictions.

[2] The United Kingdom, Ireland, Canada, United States, Australia, and Israel have a common-law tradition (Israel is regarded as a mixed system, but in the area of planning and property law it resembles other common-law systems with former British influence). For an analysis of the constitutional protection of property in these countries, see Alterman (2010, 26–35).

When Labor returned to power, it enacted the 1967 Land Commission Act along with a new far-reaching plan: in the long run the national Land Commission would assemble a large national land bank by compulsorily purchasing all land coming in for development. In the short run, a 40 percent betterment levy was imposed on all land transacted on the open market, and the levy‘s rate was to go up gradually. The revenues were to go to the central government. However, this act too was repealed by the Tories, who came back to power in 1971 (Grant 1999; Lichfield and Darin-Drabkin 1980, 144–145; Tiechelar 2003).

Labor‘s last attempt (so far?) to institute a direct tax on the betterment value was made in the linked acts of 1975 and 1976. The 1975 Community Land Act was a local-government-based version of the Land Commission Act. It would have ultimately made it mandatory for local authorities to purchase all development land (Cornfield and Carnwath 1975; Lichfield and Darin-Drabkin 1980, 169–191; Tiechelar 2003). In the interim, the 1976 Development Land Tax Act (DLT) instituted an 80 percent charge on the betterment value. This time the municipalities were allowed to keep some of the tax revenues, but most still went to central government. A team of researchers commissioned to evaluate the DLT in ―real time" found that its partial implementation was due to the lack of financial incentives for local governments to administer the tax effectively (Barrett, Bobby, and Stewart 1979; McAuslan 1980, 118–142).

The Tories kept the DLT in the books for a few years, making it the longest-surviving postwar betterment tax in Britain. However, the Tories broadened the exemptions clauses so much that the tax gradually became ineffective and was formally abolished in 1985 (Denyer-Green 1998, 274–275). Since then, Britain‘s policy has so far said ―no" to betterment capture.

However, the issue is by no means dead. In 2004 the Labor government commissioned the Barker Report, which recommended reintroduction of a mandatory national betterment levy to be called the Planning Gain Supplement. It would have captured 20 percent of the increase in land values resulting from the grant of planning permission. This proposal was rejected, partially because developers feared that the indirect value capture would continue in addition, and partly because local governments would not have been the direct recipients of the proceeds.[1]

Instead of going dramatically back to the tradition of direct betterment capture, the Labor government preferred a hybrid type of levy—a graft of direct and indirect value capture called the Community Infrastructure Levy (CIL). Ironically, the new levy was to commence on April 6, 2010, on the eve of the national elections. The levy would be discretionary, based on a preset formula that reflects the additional floor space allowed by a planning permission rather than the property‘s additional value. There is flexibility in the types of infrastructure that may be financed by the levy, and the geographic range is broad. However, the new levy specifically excludes affordable housing, to continue to be delivered by means of ―planning obligations" negotiated with developers—a well-established type of indirect value capture extensively used in the United Kingdom (Crook et al. 2002; see also section 6 of this paper). The Conservatives who gained power in the May 2010 elections had declared all along that they would abolish the levy, and the new cabinet decided to review is.[2] Will the fate of the CIL be even more short-lived than its historic predecessors?

With this history, no direct betterment recapture policy (meaning, no Labor government) has yet lasted long enough for evaluation research to provide evidence for future policy makers. Since all betterment policies were adopted by Labor yet were altered by Labor itself at the next opportunity, it is clear that none were deemed good enough for re-adoption. Nevertheless, the British experience does provide some tentative lessons about why betterment capture policies may not work, to be summed up in section 5.

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[1] UK Department for Communities and Local Government (2008). ;

UK Department for Communities and Local Government (2010).

[2] Report to Cabinet Title: Community Infrastructure Levy Regulations (CIL) – (Proposals to Replace S106 Planning Agreements) – Update Following Government Consultation,

May 27, 2010, http://www.rbwm.gov.uk/public/meetings_100510_peosp_community_infrastr_levy_regs.pdf.

4.4 Israel: A Sustainable Betterment Levy

Israel's experience with betterment capture is the longest-lasting current policy among the sample countries (or reported in the international literature). The betterment levy dates back to the 1930s during the British administration over the region. Like many other former British colonies and protectorates, Israel imported unworkable notions of a betterment tax similar to the old British laws. But in 1981, an extensive revision to the betterment tax was enacted that sets out clear and workable rules for levying the net betterment derived from land-use decisions. The law also provides several types of socially based exceptions, including deprived town and neighborhoods, urban regeneration areas, and individually built homes of modest size.

All local planning commissions are obliged to levy 50 percent of the real increment in land value, to be assessed parcel by parcel. Three types of planning and development-control decisions are the legal grounds for the levy: approval of a local or detailed plan, approval of a variance, and approval of a nonconforming use. A bill submitted to the Knesset in April 2010 would add approval of a subdivision plat. The law wisely separates out the grounds from the occasion for levying so as to avoid the mistakes of the old British legislation. The levy is paid upon the sale of the property or application for building permission. Importantly for a country where nationally owned land is more prevalent, the levy applies to both private land and public land on long-term leases (which in Israel function almost like freehold land; Alterman 2003).

In addition to the compulsory betterment levy, Israel also imposes a 25 percent unearned increment tax upon sale of a property to tap the added value in general (not necessarily linked to land-use decisions). Sale of a private residential unit is usually exempt. When both the betterment levy and the unearned increment tax apply, the two are offset against each other.

The Israeli betterment levy is an important though highly fluctuating source of income for local governments. Its success is partly due to the fact that the municipalities keep the full proceeds. However, this type of levy is not free of distributive-justice issues. On the intermunicipal level, the levy is inherently uneven because the opportunities for development are a matter of ―luck," depending on a town's location, past development patterns, and vacant land. Any betterment such levy of this type would be inherently regressive because the revenues per unit of land will be higher in localities where land values are higher. The revenues are also intrinsically uneven over time because land reserves deplete whereas urban regeneration is slow to occur.

The success of the Israeli betterment levy has several additional reasons: its rationale is clear; the appraisal is plot-specific and provides for fair procedures; the rate is uniform, nondiscretionary, and high enough to justify administrative costs; there are reasonable socially based exceptions; and the revenues may be used for an open-ended set of public services. The levy has never become a major issue in national or local electoral campaigns. In addition to the betterment levy and unearned-increment tax, Israeli planning bodies also practice indirect capture mechanisms (exactions) in varying degrees (Alterman 1990, 2001, 2007). The Israeli example thus shows that, where the real estate market is vibrant, land values may be able to tolerate cumulative layers of value capture mechanisms.

4.5 Poland: A Nonoperational Betterment Levy

Poland too currently has a direct betterment capture mechanism. In the 1990s, after the demise of the Communist regime, Poland legislated a new planning law that introduced a levy on the betterment value created by the approval of an area plan. In view of the strong private property ideology that prevails in Poland, the adoption of the betterment levy at that junction was not a trivial decision. However, the levy as instituted was in fact destined to be barely operational. The legislators should have looked more closely at other countries' experiences in order to avoid repeating mistakes.

Some aspects of the Polish levy are potentially robust. It taps only the real value increase by requiring parcel by parcel appraisal, and the local governments in charge of collection are also allowed to keep the revenues. But several factors weaken the Polish levy. First, the Polish legislature anchored the levy in the approval of a local land-use plan even though such plans did not

exist at the time, and still cover only a minority of the country. Most development decisions are granted by means of ad hoc development permits to which the betterment levy does not apply. Second, the law provides for a discretionary rate of between 0 and 30 percent, which may vary even within a single plan. Thus a fairness criterion among landowners is not built in. If a rate lower than 30 percent is applied, the administrative costs may be too high. Third, the law leaves gaping ―escape loops" for landowners. The Polish legislators repeated the mistakes of the British Town and Country Planning Act of 1932 by adopting the occasion of sale of the property as the only tax collection point and by stipulating a maximum number of five years beyond which the authority to tax would expire (Gdesz 2010).

Therefore, direct betterment levies in Poland exist largely on paper. When a legal framework is weak, there is room for differential application (not to say favoritism and corruption). There is currently some discussion in the Polish government about major revisions to the law.[1]

4.6 The Spanish Tradition and Beyond

Spain is another OECD country that, although not in my sample of countries, merits a quick look at its plus-value capture policy because the Spanish tradition, like the British one, has been influential beyond its borders. The Spanish Constitution of 1978 enshrines the betterment capture principle: ―The community shall have a share in the benefits accruing from the town-planning policies of public bodies" (section 47). The rate of the operative levies is about 10 to 15 percent—much lower than those of the three countries discussed earlier in this paper (Calavita and Mallach 2009; Calavita et al. 2010; Gielen 2008). Unlike Israel and Poland, in Spain the betterment levy is not necessarily assessed parcel by parcel and may not reflect the real value increments of specific plots. In addition to direct betterment capture, Spanish law obliges developers to finance a wide range of public services as well as to dedicate land to the municipality.

The importance of Spain extends to South American countries, most of which are not OECD members. In these countries, the discussion of the ―plus value" as it is called in Spanish, often occupies a high place in both political and scholarly discourse. Legislated instruments of various types have been enacted (Furtado 2000; Smolka and Furtado 2001, 2003; Smolka and Amborski 2007). However, the evidence shows that actual implementation is weak due to the rampant informal development and other administrative and governance weaknesses. Smolka and Amborski's (2007) comparative assessment of South America and North America leads to the conclusion that the former is very strong in rhetoric about direct value capture, while the latter shuns direct value capture but is strong on indirect value capture mechanisms.

What about the other advanced-economy countries not included in my sample? Because the sample of OECD countries is large and varied, my tentative assessment is that not many other OECD countries practice direct betterment capture. In developing countries, where public administration is often weak, even where such levies are on the books (perhaps as relicts from former colonial status), they are unlikely to be effective in practice.

5 Distilling Lessons from the International Experience

Why have most countries avoided adopting direct betterment capture policies? Unless each country insists on making its own mistakes, the experiences gained by Britain, Israel, and Poland should be mined to draw out the relevant lessons. In the absence of any comparative empirical research on outputs, outcomes, or impacts of betterment capture policies, I shall rely on the tentative observations based on the analysis presented earlier. Here are some observations:

[1] Based on personal conversations with Polish government representatives during two visits as a guest of the Polish government in spring and summer 2009. Based also on ongoing conversations with Dr. Miroslaw Gdesz, an administrative court judge in Warsaw.

- The rationale for plus-value policy is not as easy to “sell” to politicians and voters as may seem from the logic of the argument. The British experience is a real-life laboratory of how the absence of political support can lead to the rise and demise of betterment capture policies along with shuffles in the ruling parties. To adopt a successful betterment-capture policy, proponents must be able to package a rationale that transcends party ideologies. This of course is no easy task, but it is a sine qua non. In the Israeli and Polish cases, the betterment tax has not been a party-political issue and thus has escaped the tug-of-war that its British counterparts have experienced.
- One of the arguments used against direct betterment-capture policies is that they may raise real-property prices because the price of land component would rise. If that were true, it would erode some of the justification for recapture policies. The British experience has not generated much evidence on this issue despite the experimentation with a broad range of tax rates. All of Britain‘s direct value capture policies installed between 1909 and the mid-1980s were too short-lived to enable systematic evaluation. Nor has the Israeli experience delivered reliable empirical evidence because the 50 percent rate has been uniform over time and place (unless exceptions apply). Thus there has never been a “control group” to analyze. The scholarly literature on related taxes and exactions indicates that their effect on property values depends on a variety of extraneous market and contextual variables (Skaburskis and Qadeer 1992; Evans-Cowley and Lawhon 2003). Empirical research has shown, for example, that the impact may differ between raw land and built-up areas and that these may offset each other (Ihlanfeldt and Shaughnessy 2004). Since the authority to tax must usually be derived from primary legislation and applied equally, policy makers have little flexibility to adjust the level of the levy and its grounds to accommodate market fluctuations. In considering betterment capture it is important to conduct as much prior economic modeling as feasible (see also Vickars 2003).
- The British experience also teaches us that in order to sustain a betterment capture policy; there should probably be a direct link between the government authority charged with collecting the tax and the one that benefits from the revenues. Research evidence conducted in “real time” during the life of the last British recapture policy in the latter 1970s indicates that when local governments had a lesser interest in the revenues, collection was not robust enough. In the Israeli and Polish cases, the levy is administered and kept by the local governments, and they have been its major watchdogs.
- In order to retain public support, the legislation should determine in advance which public services may be financed by the levy and should expose this to the public. However, there is built-in tension between this objective and the need to maintain flexibility to accommodate changing needs for public services or changing public perceptions about what services merit public support. The traditional services such as linear infrastructure and educational facilities may compete with newer items on the list such as environmental conservation, historic preservation, or affordable housing. There are always many mouths to feed, while the potential income from a betterment levy is finite. It is difficult to “square the circle” and resolve this inherent tension between earmarking and flexibility.
- Developers are likely to argue that the revenues should be reinvested in public services for the benefit of the project that generated the funds. This argument should be resisted because it turns betterment recapture into an indirect value capture instrument with a rationale based on mitigation of negative impact or on indemnification of a burden on public services. If so, this type of value capture policy should be designed from the start as an indirect value capture instrument with an impacts-based rationale at its forefront.
- To retain its rationale, the betterment levy should be assessed parcel by parcel so as to capture only the real rise in value, as successfully applied in Israel (and potentially in Poland). However, this raises the administrative costs significantly. To allow a reasonable net yield, the rate of the levy must be relatively high. Public agencies might be tempted to

simplify the levy by adopting a preset charge based on some easy formula (such as per built-up area of per assumed average increase). This type of quasi-betterment levy was briefly proposed in Israel in 2006 but discarded following protest by the Association of Local Governments. Some scholars have recommended similar formula substitutes (Ihlanfeldt and Shaughnessy 2004; Gdesz 2005 for Poland). Such shortcuts gnaw away the very rationale of direct value capture and, with time, might lose the value capture justification and become just another tax.

- Direct value capture poses a tough distributive justice dilemma. Adoption of a uniform rate for all landowners and locations is fair in some ways but not in others. Although the rate may be ostensibly equal, the opportunities for revenue are never equal across place and time. Betterment levies also have inherent regressive attributes. Well-off towns where property values are usually high or where land reserves happen to be available will be able to reap higher revenues than less-advantaged or just historically unlucky towns. Thus an equal assessment rate by no means ensures equal revenues—by whatever indicator chosen.
- Finally, a similar ethical dilemma applies to the distribution of the revenues. On the one hand, the desire for local voter support justifies retention of the full revenues at the local level. But on the other hand, distributive justice considerations justify redistribution. Localities with high revenues do not necessarily need or merit the revenues most. Calibration of funds among municipalities could be done by means of the national or regional governments on the basis of various criteria. Two of the British postwar policies as well as the 2005 rejected proposal did incorporate a national-redistribution policy. However, these policies are deemed to have failed partly because they paid a price in lost local public support and in reduced efficiency in tax collection. This dilemma faces issues of both ethics and feasibility, and there is no sure and tested way to resolve it.

The fact that most countries have not adopted a direct form of betterment capture indicates that the shortfalls and dilemmas noted here are not easy to resolve. There are many built-in catch-22s and very little international experience from which to learn. Meantime, the indirect value capture instruments have been flourishing.

6 Indirect Value Capture

Even though direct betterment capture is not prevalent, the idea that government should reap the unearned increment on land has not died away; it has simply undergone various mutations. The need for innovative funding sources for public services has in fact increased in recent years. There are three well-known reasons for this increase: growing voter reluctance to pay higher taxes, higher costs of many services, and—at the same time—voters' expectations for amplified services (Alterman 1988b; Altshuler and Gomez-Ibanez 1993, 1–4; Callies and Suarez 2003; Rosenberg 2006; Nelson et al. 2008, iv–xiv; 1–3).

Local governments therefore increasingly need to conjure up financial instruments that are less visible to voters than direct taxes or levies. The alternative is to leverage local governments' authority to regulate land use, and solicit from landowners or developers money, land, or construction services in exchange for an affirmative decision or fast-track processing. But instead of doing so through the front door of direct betterment capture, local governments in many countries increasingly adopt a smorgasbord of indirect value capture instruments.

6.1 A Variety of Terms and Instruments

Indirect capture instruments vary from country to country and locality to locality. They are known by a variety of terms. A general term proposed by Alterman and Kayden (1988) is *developer obligations*. In the United States indirect value capture instruments are generically called *exactions*. In the United Kingdom they are known as *planning gain*, or, more recently, *planning obligations*. In France the term is *participation*. (Renard 1988). If based on preset formulas indirect instruments

may be called *impact fees* in the United States or *development charges* in Canada (Slack 2004). In the Netherlands the term (as translated into English) would be *cost retrieval* or *cost allocation*.[1] The term *incentive zoning*—born in the United States but of recent international spread—refer to two-tier discretionary instruments whereby the developer may choose to grant the desired good or obtain lesser development rights.

6.2 Alternative Rationales for Indirect Value Capture

How do indirect value capture instruments relate to the direct ones? The same generator propels indirect and direct value capture—the increase in land values due to land-use decisions. However, the unearned-increment rationale remains only in the background. Under some legal regimes, such as the United Kingdom, to survive legal scrutiny, users of an indirect instrument may even have to prove that they are *not* motivated by the desire to recoup ―betterment by stealth."[2] Alternative rationales must be conjured up. I propose the following classification (compare Healey, Purdue, and Ennis 1993):

- Indemnification of direct public costs of public services generated by the particular project (―cost recovery"). In cases where cost recovery is capped by the amount of betterment, the instrument becomes a hybrid between direct and indirect value capture.
- Need for public services, infrastructure, housing, or ecological services that are not met by the market or by existing funding sources.
- Internalization of negative externalities such as noise, radiation, or pollution.
- Mitigation of impacts on the natural environment or on historic buildings.
- Mitigation of perceived social injustices such as social exclusion or higher housing prices.

In practice, a mixture of these rationales may serve as the legal or public-policy ground. Real-life application of indirect instrument often contains ambiguities about which of the alternative notions is being applied in a particular case. Indirect instrument also vary in how the contribution is delivered: some are in money, others in kind whereby the developer constructs a public service, delivers mitigating technologies, supplies land, or builds housing.

6.3 An International View of Indirect Value Capture

Among the sample of thirteen OECD countries, all except Sweden and the Netherlands have decades-long experiences with shifting the costs of public services onto developers. Since the 1990s Sweden too has been gradually joining the group. The Netherlands is the last in the set to adopt indirect capture instruments, formally enabled for the first time by the 2008 Land Act. So even the Netherlands—with its uniquely strong tradition of direct government action in land purchase and development—must now rely more and more on land-use regulation and private developers as a source of financing for public services (Needham, 2007, 176–177).

Indirect instruments differ from direct ones in the way they emerge. Direct capture instruments are usually enacted or otherwise adopted ―top down," often for an entire jurisdiction. This is because in well-governed countries, authority for direct value capture may entail special enabling legislation (at times even constitutional amendments). By contrast, indirect instruments often emerge ―from the bottom," by dispersed locally grown policies. If the instruments are viewed as successful and survive legal challenges, they are likely to be copied by other localities. The United States has been an especially rich breeding ground for a wide variety of innovative value capture instruments that

[1] These are the official terms in the English translation of the Dutch Land Development Act that came into effect in July 2008. Available at http://www.vrom.nl/docs/internationaal/Land%20Development%20Act.pdf.

[2] The official UK government circular on ―planning obligations" states in section B7: ―Planning obligations should never be used purely as a means of securing for the local community a share in the profits of development, i.e. as a means of securing a 'betterment levy.'" (July 2005 Circular 05/2005, Office of the Deputy Prime Minister).

are recently being ―exported" overseas (Alterman 2005; Spaans, van der Veen, and Janssen-Jansen 2008, 17–22).
Because the indirect instruments are usually locally determined and may not require explicit legislation, they have several advantages over direct betterment capture:

- They can more easily go ―under the radar" of party-political debates and can therefore better survive changes in party ideology and voter resistance to new taxes.
- They can more easily be justified to the project‗s consumers and to the general public if they are linked to the burden that the project would have otherwise placed on the public.
- They are more flexible for financing changing public needs because they are usually applied only when development is ripe.
- They can be fine-tuned to be politically more acceptable when sociopolitical positions change in the community
- They may be adjusted to accommodate the changing economics of real estate so as not to drive away development.

Yet, indirect capture instruments are not a panacea. They are often applied case by case, without ensuring equality among landowners. These instruments are therefore open to political and legal challenges regarding bias and favoritism. The value of the financial or in-kind resources delivered by developers is often unpredictable because it depends on uncertainty about estimates of anticipated impact or on the success of negotiations. The extent of financial gains to the community may vary even among parallel projects. There is some evidence that the financial gains to the public may represent only a few percent of the unearned increment (Alterman 1988a).

6.4 Some Preconditions for Adoption of Indirect Value Capture

Indirect value capture policies are likely to expand and intensify around the world. Because of the complexity of these instruments, there is great need to exchange knowledge between jurisdictions, so more systematic comparative analysis is necessary. I hypothesize four preconditions for reasonably successful application of indirect modes of value capture:

- Governments should have well-trained professionals (planners or real estate experts) to negotiate with the developers or to develop preset formulas of impact assessment. The professionals need to be savvy in real estate economics to be able to assess the limits of how much may be exacted from the developer without ―killing" the projects.
- Local government should conduct good monitoring of fluctuations in land prices in order to be able to challenge developers‗ arguments that the exactions in fact raise the cost of housing or other products. This type of argument—not necessarily true in specific market situations—may generate public opposition.
- There should be enough transparency in negotiated exactions to help withstand legal challenges (yet full disclosure is often not possible in order to protect the legitimate economic interests of the developers).
- Countries or local authorities known for high levels of corruption should refrain from adopting value capture instruments with discretionary elements. A reasonable good level of trust in government is a precondition for their successful operation.

7 The Future of Direct and Indirect Value Capture

An obvious issue is the interrelationship between the two categories of value capture. In those few countries that do practice betterment capture, does it in fact replace the need for indirect capture instruments? The state of current knowledge does not provide empirical answers to this question, and the body of law is also skimpy. However, the underlying logic of the two modes leads me to conclude that they are not mutually exclusive. The indirect capture instruments are often open-

ended and evolving, and they possess the capacity to ―fill in the holes." So long as governments have insufficient resources for public services (as they often do) and so long as they have the authority to refuse permission to develop, indirect value capture, especially its negotiated modes, is likely to be practiced to some extent.

The experiences of the United Kingdom and Israel shed some light on this issue. In Israel, negotiated exactions are sometimes applied over and above the 50 percent betterment levy, and case law has not ruled them illegal. In the United Kingdom, negotiated planning gain (today called ―planning obligations") likely existed to some extent in parallel to the various direct betterment capture modes exercised until the early 1980s. The current debate surrounding the 2010 Community Infrastructure Levy illustrates the difficulties of drawing a solid boundary between the two modes of value capture. Although the policy statement makes an effort to restrain double charging, developers and the new Tory-led government are not yet convinced.

The bottom line is that the rationale for direct betterment capture may be convincing on paper, but it has not caught on widely across the world. At the same time, indirect value capture tools have proliferated. As counterintuitive as it may seem to those who have not walked through this paper, these instruments—with their ―messy" rationales and exposure to legal challenges—hold the more realistic potential for funding public services than their elegant direct-capture siblings.

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