

# Regional Plan Association

**FUNDAMENTAL PROPERTY TAX REFORM:  
LAND USE, REGULATORY AND FISCAL REFORM**  
Sponsored by Regional Plan Association and the Lincoln Institute of Land Policy

SUMMARY OF ROUNDTABLE 1  
*How Can We Afford Smart Growth?*

Convened on Wednesday, February 23, 2005  
Edward J. Bloustein School of Planning and Public Policy  
Rutgers University  
New Brunswick, New Jersey

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On February 23<sup>rd</sup>, Regional Plan Association and Lincoln Institute of Land Policy hosted the first of a series of panel discussion exploring the relationship between fiscal policies and the landscape in which we live. The panel, entitled “How Can We Afford Smart Growth?”, explored the financial obstacles to realizing smart growth, and raised suggestions about how to overcome these barriers.

RPA President Bob Yaro and Lincoln Institute for Land Policy Senior Fellow Armando Carbonell welcomed the 60 or so participants and described the goal of the day’s panel: to better understand the land use implications of the current system of taxing and spending, and to move the agenda of property tax reform to include ways to improve opportunities for Smart Growth. Bob and Armando referred to the roundtable briefing paper, which described how the current property tax system frustrates Smart Growth:

- Over-reliance on locally-collected property taxes causes municipalities to compete for fiscally positive development at the expense of other planning goals.
- Because the most lucrative developments tend to be commercial and industrial uses, while residential uses tend to be a net loss, municipalities over-zone for commercial uses and under-zone for residential uses. This leads to a diminished supply of housing, higher housing costs, leap-frog development, and loss of open space.
- In the long run, this system does nothing to avoid higher property taxes, as development inevitably creates additional costs, forcing local officials to choose between raising taxes and encouraging more development. The cycle eventually ends as municipalities become built out, with no recourse but to raise taxes as costs of development come due.

The briefing paper can be accessed from the New Jersey webpage online at [www.rpa.org](http://www.rpa.org).

Yaro and Carbonell pointed out that in order to make Smart Growth the development pattern of first resort, it must make financial sense from the point of view of developers, local budgets, the state budget, and taxpayers. It was with this in mind that RPA and LILP brought together experts from diverse fields to discuss the current situation and opportunities for reform. What follows is a summary each panelist’s salient points.

## **The Big Picture: The Historic and Economic Context for Property Tax Reform**

Dean James Hughes and Dr. Joseph Seneca provided a framework for discussion by putting the problem in historic and economic context. Dr. Hughes described how today's landscape is the product of six decades of residential suburbanization, five decades of retail decentralization, and two-and-a-half decades of office development. While each wave of growth may have made sense to local governments in the short term by providing infusions of revenue, in the long term this growth has been accompanied by rising property taxes and fiscal stress. Jim's presentation demonstrated that we need to think about what is affordable over the long term and design fiscal policies and investment strategies to support these ends. This means considering the demographic changes that will drive the next wave of growth -- including more young people and more immigrants moving to the suburbs -- as well as the infrastructure investments that shape development.

Dr. Seneca put the problem in a larger economic and fiscal context, arguing that any proposed property tax reforms must be affordable for the state as a whole. Joe said that the property tax problem is often understood as too-high property taxes and a too-heavy reliance on local sources of revenue. As such, the most commonly proposed solution is to shift revenue from local sources to the state. This proposal ignores the fact that the state already has a structural deficit of \$4 billion dollars. Reducing the current property in a meaningful way will require significantly raising state taxes and/or cutting expenditures, which will mean cutting services. For example, reducing property taxes by 50% will require finding at least \$8 billion in additional revenue. With these realities, a fiscally responsible and sustainable solution to high property taxes will require expenditure reductions as well structural reforms.

## **The Private Sector Costs of Smart Growth**

Bill Tucker described the difficulties of financing individual Smart Growth projects. He pointed out that, even for developers who are committed to Smart Growth, there are real obstacles to realizing these projects beyond those faced by traditional developers. The obstacles and opportunities that he identified included:

- Planning should reflect market realities.
- Regulations need to support Smart Growth. Developers often have to spend time to get zoning changed, which raises the costs of Smart Growth.
- The fragmented regulatory structure frustrates Smart Growth. There are over 500 municipalities, each with its own codes and regulations -- streamlining this system would go a long way toward making Smart Growth affordable. The state could help by providing model regulations and ordinances that could be easily adopted by local governments.
- Finding financing for Smart Growth projects is a challenge. Typical investors are primarily interested in short-term returns, but Smart Growth projects make money over the long term. New "patient" sources of investment are needed. Local governments could be a source of "patient capital". This would provide developers with investment, as well as a public-sector partner committed to the success of the project. Local governments would get the social and environmental benefits of smart growth, and would benefit financially as the project made money over the long term.

## **Municipal and County Issues: The Case of the Somerset County Regional Center**

Rob Lane presented RPA's recent work in Somerset County to connect the Regional Center's Vision to the fiscal realities and infrastructure needs of the center. He pointed out that, while the Somerset County Regional Center has had real success, obstacles to full implementation remain. These include:

- Responses from developers have been relatively weak.
- Taxpayers are concerned about proposed increases in density because of the costs associated with additional development, in particular residential development.
- Specific infrastructure projects are quite costly. Existing sources of public investment are inadequate.

Lane focused on a particular redevelopment project along the Route 22 to show how some of these obstacles could be overcome.

- Projects need to be carefully designed from both a fiscal and an aesthetic standpoint. By mixing commercial and residential development, Rob showed that the development plans for Route 22 will be a net fiscal gain for Bridgewater (the town in which it is located). Demonstrating the positive fiscal impact of development should allay local concerns about density.
- Lane showed how redevelopment of Route 22 could absorb much of the anticipated growth from the environs outside of the Regional Center. Focusing commercial development along Route 22 could save about 1,000 acres of open lands outside of the Regional Center. Smart Growth is more likely to be acceptable if the connection between higher density in areas appropriate to growth and open space preservation is made clear to the public.
- Good design and public education will only go so far in the current regulatory environment. In order to get taxpayers and local officials to more readily accept higher density residential development, it is necessary to reform the property tax and school funding systems.

## **Potential Reforms from an Economic Perspective**

Dr. Paul Gottlieb reviewed fiscal analysis he completed for RPA as part of the Somerset Regional Center Initiative. In his discussion, Gottlieb explicitly linked fiscal reforms to land use incentives, and described several issues that need to be examined to sort out the impacts of proposed solutions.

- There are essentially two types of finance tools: those that subsidize development, such as tax abatements, and those that tax development, such as tax increment financing. The first is appropriate for "weak market" conditions and the second for places where market conditions are strong enough to carry the additional costs.
- While ratable chasing has received most of the attention from Smart Growth advocates, "ratable shunning" – a local no-growth attitude – is equally prevalent and needs to be considered in enacting fiscal reforms.
- Paul reminded the audience that developers are risk-averse. In order to prove to developers that Smart Growth can be cost effective, public sector demonstration projects must be undertaken. Although it may be politically difficult to invest a significant sum in one place in New Jersey, he nonetheless recommended that the Somerset Regional Center be designated a demonstration project to jump-start state-wide redevelopment according to Smart Growth principles.

- Gottlieb noted that, with the exception of research into a pure land tax, little academic literature exists on public fiscal systems to promote land use policy. Paul suggested further research on the idea of a tax on new construction according to planning areas in the State Plan (first identified in the report of the State and Local Expenditure and Revenue Policy Commission (SLERPC) in the mid-1980s).
- Gottlieb also pointed out that how state aid formulas are structured can have a big impact on local tax and land use incentives. Research is needed on what formula of State aid would best reduce the ratables chase, and whether matching or lump-sum grants could play a factor.

### **Political Realities: A Response from Legislators**

Two legislators provided responses to this program, Senate Minority Leader Leonard Lance (R-23) from Hunterdon County, and Senator Bob Smith (D-17) from Middlesex County, who chairs the Senate Environment Committee and was the key sponsor of the Highlands Water Protection and Planning Act.

Senator Lance pointed out that Smart Growth cannot occur without a meaningful discussion on property tax reform, which in his opinion requires constitutional caps on spending at the local level, especially for the school districts. He noted that unless spending is addressed, tax relief will be temporary and taxes – including sales and income taxes -- will inevitably rise again over time. Senator Lance believes that property tax reform can be achieved via a special session or property tax convention, which should deal with both taxing and spending.

Senator Smith also made the connection between Smart Growth and property tax reform. Senator Smith pointed out that, under the current system of locally funded and locally-controlled schools, taxpayers and local officials shun any development likely to bring more children. Senator Smith argued that, in order to lift the burden of property taxes, you need to go where the money is – this means cutting the costs of education by delivering education services in a more cost-effective way. To address this problem, Smith proposed consolidating the state’s 616 school districts at the county or regional level to reduce the costs of education. (Senator Smith goes into more detail about this plan in an article he handed out entitled “Another Way to Reduce Property Taxes.”)

Tom Dallessio summarized the key points heard during this first panel, pointing out that at all levels at which we talk about “affording smart growth” -- from a single project financed by a developer, a regionally-important long-term redevelopment project, municipal budget, state budget – there are real challenges, one of which is the current property tax system. However, as we saw at this discussion, there is also real interest in overcoming these challenges, and real opportunities for reform.