

Response to “Impact Fees and Housing Affordability” by Vicki Been

William A. Fischel
Dartmouth College

Professor Vicki Been has provided an excellent survey of what we know about impact fees. Her economic analysis is sound and well balanced, and she has surveyed the major works in this area with insight and institutional nuance. Her call for empirical work that takes into account the benefits, as well as costs, of exactions is especially important to heed. To that end, the focus of this comment is why thinking of exactions as fees for service rather than as taxes is better. Been’s analysis presents both views about the nature of exactions, but she leans toward viewing exactions and impact fees as prices. I want to second that inclination and explain why it matters.

A tax is an obligation imposed by the government on owners of assets and income streams within its jurisdiction. Most taxes are uniform in their effect in this minimum sense: they treat people and assets that are economically identical the same. In this respect alone, it could be argued that land use exactions are different from taxes in that similar activities can easily be subjected to different exactions. Exactions are sometimes negotiated with government officials, and, for what are often legitimate reasons, different developers may end up paying different exactions for otherwise similar projects.

Uniformity, however, is not the key difference between exactions and taxes. The most important difference is that taxes are not directly connected to an entitlement to some government benefit. A person who (legally) pays no federal income tax because he/she does not earn sufficient income to be taxed is nonetheless entitled to all the services that the federal government offers its citizens. Someone who owns no property in a locality and, is thus, nominally, not subject to property taxation still is entitled to send his/her children to local public schools, use the roads and parks, and participate in public life on the same terms as everyone else. Of course, one can say that such a person indirectly pays taxes as a renter, but that merely shows that a direct link is not required between taxes and government services. Paying more taxes generally does not get you more government services.

Now, contrast the taxpayer with the development-minded landowner who wants to obtain permission from zoning and planning authorities to build something. This person may face a schedule of impact fees or an ad hoc group of land use exactions—some in cash and some in kind. If the would-be developer declines to pay these exactions and fees,

he/she will not receive his/her permits. Period. The ability of local officials to conditionally withhold a permit is the essence of an exaction, and this ability is what makes exactions different from taxes.

Taxes and fees intersect at two points that further illustrate their fundamental differences. One is the aphorism of Justice Oliver Wendell Holmes, Jr., that “taxes are what we pay for civilized society.”¹ The unstated, but clear, implication is that those who decline to honor a legal obligation to pay a tax will not get to enjoy the benefits of civilized society. They will, instead, spend time in jail. The benefits of civilized society, however, are available to all who pay their taxes, regardless of their amount. These benefits also are available to those who arrange their affairs—say, by emulating Henry David Thoreau’s 2 years at Walden Pond—so that no taxes are due. Conversely, the benefits of civilized society still are available to development-minded landowners who decline to pay impact fees. All they forgo is the building permit. They are not put in jail or refused service by the police and fire departments.

The other intersection between exactions and taxes arises when people have a choice of jurisdictions. If a potential resident or property owner has not settled on any particular community in an area with many to choose from, the combination of local taxes and local services can be thought of as a menu choice. In this context, the difference between exactions and taxes becomes less clear insofar as the potential resident views what the revenues finance—schools, police, fire, parks—as being paid for by the prospective property taxes that he/she will pay. Likewise, a property owner who has already purchased land in a community cannot avoid the adverse effect of a change in property taxes or exaction policies by selling his land and moving away. The buyer, in either case, will have notice of the change and will adjust the amount he/she is willing to pay downward by the net present value of the burden.

The remaining difference between exactions and property tax burden in the Tiebout model (the name political economy gives to the situation in which communities are numerous) is what may be called the majoritarian problem. Exactions often are ad hoc and nonuniform. That gives greater scope for the majority of local residents to extract some economic surplus (land rent) from individual owners who seek to develop their properties. The uniform assessment and rate conditions imposed on local property taxation deter much of this opportunistic rent-seeking. A local official who proposed that all land—developed or not—should be subject to a confiscatory tax (à la Henry George) would, in most instances, find that his/her tenure in office was brief. But an official who proposed that all owners of undeveloped land would have to pay exactions of a similar magnitude would often enhance his/her chances of re-election, especially in places where owners of undeveloped land were few in number and not resident to vote.

The point of this digression about the difference between exactions and taxes is that exactions have to be examined in a fashion different from that of taxes. With taxes, one can ignore, in most cases, what the tax finances. This allows for the usual partial-equilibrium graphical analysis of tax incidence that Professor Been demonstrates that she has mastered. But as she notes—though not prominently enough for my taste—this approach seldom fits the usual exaction scheme. As a result, the tax analogy can lead to counterproductive recommendations. Viewed as just another tax, exactions would seem solely to raise housing costs, and affordable-housing advocates would want them reduced.

When exactions are more properly viewed as a fee for service, however, a policy of reducing exactions is far more problematical. If seemingly high local exactions are reduced by state or federal legislation, the response of the communities affected must be

taken into account. The localities can, in the exactions case, withhold development permits that they might otherwise have issued. The effect of this supply reduction, if widespread, would make housing in the area less affordable rather than more affordable.

Yet, as Been again properly points out, this possibility does not warrant a completely hands-off policy with regard to exactions. Because of the majoritarian problem, some communities may be using exactions unfairly to finance public expenditures that should be borne by all property owners, not just those who were last to approach the moat. Purely rent-seeking exactions (those that try to divert some of the developer's capital gains to the community) are not, in theory, harmful to the development of affordable housing (Fischel, 1987). Rent-seeking by the community, however, often induces landowner-developers to adopt counterproductive strategies. For example, a large-scale developer might refuse to pay exactions, hence leaving land undeveloped, to establish a credible threat in a later round of negotiations with community officials. Beyond that, the perception that being a developer reduces one's stature in the law surely deters many decent people from becoming developers or dealing with especially aggressive communities. The theory that communities can selectively extract land rents from one set of the population is actually dubious as a practical matter, and that translates into less affordable housing.

The other problem that Been points to is that some communities enjoy a monopoly-like position with respect to development. This may be because of some natural resource advantage, such as a particularly nice lake, or because the boundaries of the municipality are so large that alternative sites in different communities are not a realistic choice. In this situation, high exactions may be like the excessively high prices that a commercial monopoly can charge because of its lack of competitors.

One should not necessarily rush to the conclusion that reducing exactions should be the focus of promoting affordable housing, even in the monopoly community. Most of the "profits" of living in a monopoly community are enjoyed by homeowners, who can eventually sell (or borrow against) their ever-more-valuable homes. Capital gains by homeowners in such communities can be had by either charging extra-high exactions for development permits (thus reducing local taxes or further enhancing local amenities) *or by refusing to issue new permits*. The monopoly on issuing building permits is the most valuable resource for the truly exclusionary, monopoly-like community. To tell such communities that they may not charge high exactions for the few permits they do issue would probably result in fewer permits being issued and continued enjoyment of high housing prices by those who will eventually be on the selling end. A better approach to the monopoly community is that of conventional antitrust: break up the monopoly by encouraging formation of new communities.

This discussion is not to counsel a "laissez faire" attitude toward local exactions. It does suggest, however, that the problem of exactions is simply the visible manifestation—and often actually an amelioration—of a more fundamental problem: the community's ability to withhold development permits. I would not join with those who would say we do not need local government control of land. I would join with those who say that we need some oversight of local control of land. Local governments should not be regarded as regulatory islands. Whether the external discipline should come from higher levels of elected government or from the judicial branch is something reasonable people can differ about.

I close by mentioning one of the few regrets I have about this excellent survey. Professor Been chose not to address what I think is an effective means of disciplining local regulatory excess. The regulatory takings doctrine, as expressed by Robert Ellickson (1977) and others, would go a considerable distance in reining in local barriers to affordable housing. I have argued that federal agencies such as the U.S. Department of Housing and Urban

Development should not have a central role in developing this doctrine, but they could make some useful pronouncements about it that would encourage its use in the state courts (Fischel, 1999). Development-minded landowners should not be made to feel that they are second-class citizens in the eyes of the courts and state constitutions. We need to keep in mind that an affordable supply of housing is the product of a system that starts with landowners being able to proceed with reasonable developments without unreasonable conditions. That “reasonable” is subject to interpretation cannot be doubted, but one can question whether the only interpreters should be local officials whose constituents gain wealth from stringent regulations.

Author

William A. Fischel has taught economics at Dartmouth College since 1973, when he received his Ph.D. from Princeton. His research specialties are land use, local government, school finance, and property taxation. Fischel wrote The Economics of Zoning Laws (Johns Hopkins, 1985), Regulatory Takings (Harvard, 1995), and The Homevoter Hypothesis (Harvard, 2001). Fischel has had 1-year leaves at the University of California campuses of Davis, Santa Barbara, and Berkeley, and at the University of Washington. He is currently professor of economics and the Barbara and William Hale Chair in the Arts and Sciences at Dartmouth.

Note

1. *Compania General de Tabacos de Filipinas v. Collector of Internal Revenue*, 275 U.S. 87, 100 (1927).

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