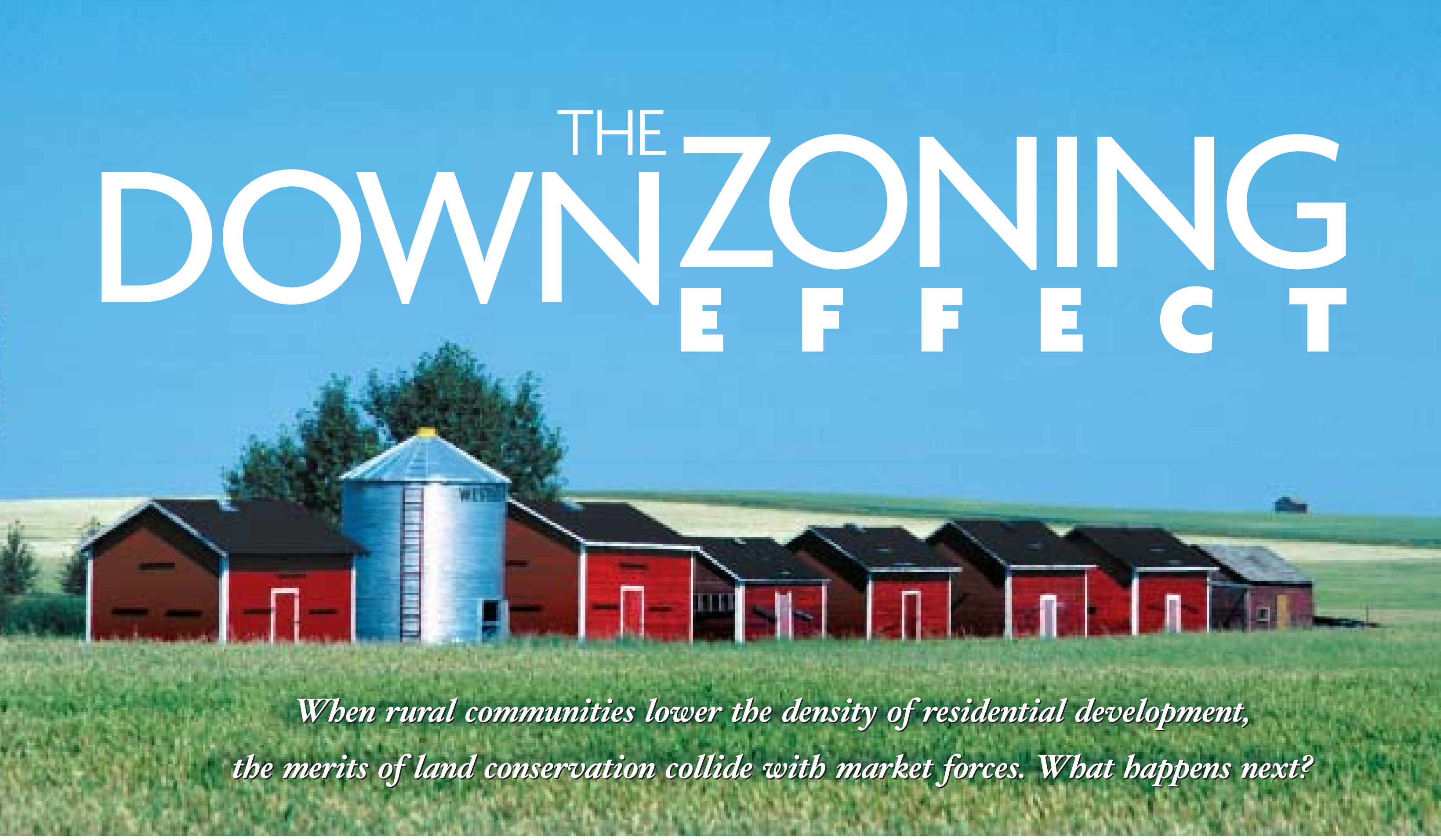
THE DOWNZONING EFFECT



When rural communities lower the density of residential development, the merits of land conservation collide with market forces. What happens next?

BY CHARLES GERENA

A middle-aged woman knits as she patiently waits in one of the hard plastic chairs lined up in the large meeting room at Cecil Community College in northeast Maryland. She has come with her husband and dozens of other residents on this April evening to learn about a proposed change in land-use management that could affect every farmer and landowner in Cecil County.

Cecil is like many rural communities in Maryland and Virginia. Its population has swelled in recent decades, more than doubling from 1950 to July 2003, according to the U.S. Census Bureau. As residential development grows, so do concerns about preserving the thousands of acres of farmland that cover one-third of the county.

In response, the local planning commission recommended changes to Cecil County's comprehensive plan in March. The recommendations included a drastic "downzoning" of two rural zoning districts.

Downzoning is the practice of restricting the type or amount of development allowed on a property. Usually this is accomplished by reducing the ratio of housing units per acre that can be built, or the allowable density of the property. In the case of Cecil County, planners want to reduce the allowable density in the northern part of the county from one house for every five acres to one house per 20 acres. They also want to lower the density in southern Cecil further from a 1-8 ratio to a 1-30 ratio.

This isn't a recent phenomenon. Twenty-two years ago, officials in Fairfax County, Va., downzoned 41,000 acres along the rivers and tributaries that feed the Occoquan Reservoir to help protect the drinking water supply. Other local governments in Maryland and Virginia have downzoned to protect environmentally sensitive areas, to prevent sprawl from gobbling up farmland, and to preserve open space. In addition, cities have implemented downzoning to keep commercial development from encroaching on residential neighborhoods.

While downzoning has been widely embraced, the practice also has been widely criticized because it can create an artificial shortage of land for residential growth as well as cause a supply-demand mismatch for private development and public infrastructure. It can also alter land-use options so drastically that landowners don't get the price they want for their property and residents don't get the development they want in the future.

Land conservation advocates like Robert Etgen counter that downzoning can succeed in preserving space while accounting for these issues. It's a matter of balancing "the benefits and burdens to the greatest number of people," says Etgen, executive director of the Eastern Shore Land Conservancy in Maryland. Any government action that restricts the use of property is going to have a cost. The question is whether the benefits outweigh the costs and how those costs are spread out.

Working Against the Tide

Localities like Cecil County are grappling with the costs and benefits of downzoning as housing development consumes a growing amount of rural land (see table). Other factors besides population growth are driving development into the countryside.

For one thing, developed areas often don't have the modern houses with spacious landscaping that people want, nor do they have sufficient land to build this type of housing.

Some blame these shortfalls on zoning policies. "Lot prices are driven up by downzoning and other restrictions on development in more urbanized jurisdictions," notes economist Anirban Basu, chairman and CEO of the Sage Policy Group in Baltimore. In contrast, "rural jurisdictions are often able to supply homebuilders with cheap lot prices."

Also, rural communities often are perceived as healthier places for families because of lower crime rates and better schools. "There is a growing number of households who are empty nesters ... free to move anywhere they want," observes Basu. Still, "more households are moving away from center cities than moving back to them."

At the same time, workers aren't as "place-bound." Michael Peddle, an economist and faculty associate at Northern Illinois University's Center for Governmental Studies, says there is a reduced need to be close to densely populated areas because "more people are able to work at home or telecommute."

Interstates enable people to reach jobs within a wider radius of their homes. For instance, 33 percent of Cecil County's residents travel over the state border into New Castle County, Del., for work.

Cecil is just one of the counties mentioned in a December 2003 report on downzoning by the Maryland Center for Agro-Ecology. The report identified several regions of Maryland as experiencing development pressure: the middle and upper Eastern Shore, which includes the counties of Cecil, Kent, Caroline, Queen Anne's, Dorchester, and Talbot; and the southern Western Shore, which encompasses the counties of Calvert, Charles, and St. Mary's. Many of these counties have either considered or implemented downzoning to alleviate this pressure. Interest in downzoning also has increased in the rapidly growing suburbs of Northern Virginia, including Loudoun and Fairfax counties.

"That's the backdrop of why jurisdictions look at downzoning; they are faced with patterns of development that are ultimately unsustainable," explains Paul Gilbert, president of the Northern Virginia Conservation Trust. "Downzoning is one way to take a broad-brush approach. It takes a large area and says, 'We're going to reduce the building potential for this area because otherwise it will be gobbled up.'"

In several rural communities, downzoning has succeeded in keeping development out of designated areas. Just north of the nation's capital, Montgomery County, Md., has remained predominantly rural due to its aggressive land management activities, which included a 1980 downzoning of more than 90,000 acres in its western and northern sections. Water quality has remained stable or improved in the Occoquan Reservoir thanks in part to Fairfax County's 1982 downzoning.

But working against the tide of market forces can cause unexpected problems. For instance, Basu says that downzoning in rural areas where government has allowed some growth to occur results in surplus public infrastructure.

"The public makes its intended investments to serve a particular area, a community forms around that infrastructure, and then community leaders ask that the area be downzoned because they are unnerved by the prospects of school overcrowding and increased traffic," he describes. If the opponents of excessive development get their way, "what you get is less dense development than had been anticipated. ... That leads to the underutilization of infrastructure."

Another problem with downzoning is that it doesn't address the unmet demand for residential development. Consequently, constraining the supply of land in one location may cause development to spread farther out, which feeds sprawl rather than curbs it.

Therefore, planning experts and land conservationists agree that downzoning must accompany other policy actions that accommodate future development in some way. These include removing regulatory barriers to denser development in urban areas, and offering redevelopment incentives.

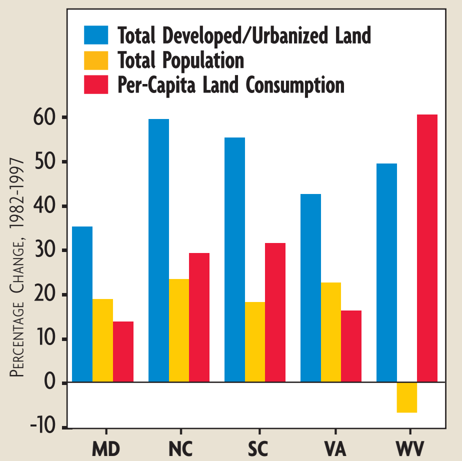
Montgomery County uses transfer of development rights (TDRs), a policy tool commonly implemented in conjunction with downzoning. When downzoning reduces the allowable density of a property, the landowner retains the right to develop at the original density in the form of a TDR. The TDR cannot be used on downzoned property, which is called the sending area. It can be used to build only in receiving areas, which are usually where development is already dense and public infrastructure is already in place. The idea is that developers will buy TDRs from landowners so that they can exceed the allowable density in receiving areas. In the process, development shifts from sending areas to receiving areas.

This Land is *My* Land

While downzoning can preserve rural landscapes, landowners are usually apprehensive about how it will affect the equity they have built up. Cecil County residents are no exception. While some support the proposed

A Growing Appetite

Over a 15-year period, every Fifth District state saw the pace of development exceed population growth. This accelerated the rate of per-capita land consumption. However, Maryland and Virginia had lower growth in per-capita land consumption, partly because they were relatively better at reigning in land development.



SOURCE: *Outsmarting Smart Growth: Population Growth, Immigration, and the Problem of Sprawl,* Center for Immigration Studies, August 2003

Getting Something in Return

All David Lucas wanted to do was make some money building beach houses on the Isle of Palms, a scenic barrier island near Charleston, S.C. He started a residential project in the late 1970s, but it came to a halt when the state passed legislation in 1988 that prohibited new beachfront structures seaward of an erosion line. Two of Lucas' lots were affected, rendering useless property that cost almost $1 million to acquire.

As far as Lucas was concerned, the state's zoning change was a "taking." Under the Fifth Amendment, landowners are entitled to "just compensation" when the government physically takes private property for public use, like a road or a school. He sued the state and won $1.2 million, then appealed a reversal of that decision all the way to the Supreme Court. In 1992, the court sided with Lucas, finding that landowners suffer a taking when a government regulation eliminates all economically beneficial uses of their property.

This sounds like an equitable outcome, right? Well, the situation gets more complicated when a government's downzoning affects the development value of rural land. Some believe that when farmers get a lower price for their land because it isn't zoned for dense development, that lost value should be considered a partial taking.

But requiring governments to compensate owners of downzoned land for a partial taking would be a mistake, according to Philip Pryde, a former geography professor at San Diego State University. "The courts, in decisions going back to at least 1922, have noted that government would be hard-pressed to function normally if compensation were required any time a decision had an adverse effect on property values," he wrote in a 2000 position paper for Republicans for Environmental Protection, a New Mexico-based advocacy group.

There are mechanisms for "achieving equity" when property values are affected by zoning changes, says Paul Gilbert, president of the Northern Virginia Conservation Trust. The owner of downzoned land could receive a transfer of development rights (TDR), which could be sold to developers to give them the ability to build in densely urbanized areas.

TDR programs help spread the cost of land conservation rather than have farmers shoulder all of it, notes Kevin Schmidt, director of the Mid-Atlantic regional office for the American Farmland Trust. "Downzoning is a very effective tool, but to be palatable to the landowner and to be as equitable as possible … you couple it with some type of incentive." —Charles Gerena

downzoning, "others, many of whom are farmers, are threatened by any attempt of government to take away their right to sell their land to a developer, claiming it is like taking away their retirement," wrote reporter Cheryl Mattix in the April 2 edition of the *Cecil Whig*. This sentiment was echoed in several letters to the editor following the article's publication.

While it seems counterintuitive to landowners, several studies claim that downzoning doesn't automatically wipe out the development value of rural property.

The Center for Agro-Ecology's report analyzed sales of agricultural land in eight counties, excluding parcels that were smaller than 20 acres, located near a waterfront or marsh, or had other traits that would skew their value. For each county, researchers averaged together land sales over a period of years, then compared the average per-acre value of land in four counties that had downzoned against average land values in four counties with similar real estate markets that didn't downzone.

"We found that, for the most part, either the acreage value was consistent between [downzoned and non-downzoned] counties or the value had increased for the county that had downzoned," says Sarah Taylor-Rogers, lead author of the report and former secretary of the Maryland Department of Natural Resources. She has explained these findings at several public forums, including the April informational meeting on downzoning in Cecil County.

Robert Gray, an Alexandria, Va.-based planning consultant who contributed to the Center for Agro-Ecology report, reached a similar conclusion in a 1991 study for the state of Maryland. His team of researchers looked at four counties that had enacted downzoning, comparing sale prices of large plots of land three years before they were downzoned and several years after to detect any changes.

Gray's explanation is that real estate markets don't always take downzoning into account when valuing a property. Although a typical middle-income subdivision cannot be developed on the site, he says that developers figure they can lobby to remove the downzoning in the future.

However, community groups have a strong incentive to lobby for keeping the zoning in place. Economist Anirban Basu says that downzoning creates an infrastructure windfall for existing residents. "There is more public capacity on a per-capita basis," he explains.

Even if the property remains downzoned, Gray believes it may still have value in the real estate market. There have always been homebuyers willing to pay a half million dollars for a nice home surrounded by a huge area of open space, he notes. (Indeed, such a buyer can find several high-dollar properties by thumbing through the *Cecil County Real Estate* guide.) According to Gray, this demand has increased as disposable incomes have increased, enabling more retirees and city dwellers to fulfill their desire to move out into the country.

In fact, there are a few examples of downzoned property becoming more valuable. Usually, this occurs when the property offers a waterfront view or other desirable natural characteristics that are safeguarded by downzoning. The initial price of downzoned land may not reflect how much people value preserving the land's esthetic qualities, notes Michael Peddle. In the long run, however, the market might recognize the value of land preservation. "In many cases, the original landowner may not be the person who ends up benefiting. It may be a subsequent landowner or a developer."

There is another possible explanation behind the studies' conclusions on downzoning and property values. In rural communities far from development, the demand for land is lower and the development potential is much smaller. Peddle says this is due to greater uncertainty about the property's future use. "If you are in the path of development, you can see the logical path of infrastructure and the demand for the land." Therefore, landowners likely have little to lose from downzoning.

On the other hand, demand is greater in rural communities that are close to densely developed communities. Therefore, the development potential of properties is higher and downzoning could result in a major loss in value for landowners.

Another study in progress will likely come to a different conclusion than those arrived at by Gray or Taylor-Rogers. Michael Samuels, a real estate consultant at Clarion/Samuels Associates in Wayne, Penn., compared properties within townships in New Jersey. His preliminary findings show that when townships increased the minimum lot size for residential development from one acre to 10 acres, land values decreased. In markets where there was a demand for 10-acre lots, the value of downzoned property fell more than 50 percent. In markets where there was no demand for such lots, downzoned property lost all of its development value.

What accounts for these differing conclusions? The Center for Agro-Ecology's study took a macro view by doing a county-to-county comparison of land values, so the negative effects of downzoning on individual properties may not show up when they are averaged together. In contrast, Samuels took a micro view by comparing land values within communities.

Samuels' approach arguably is more methodologically sound, but both studies have a hard time distinguishing "causation" from "correlation." For instance, land prices could rise in areas where downzoning has occurred, but that doesn't necessarily mean that one event led to the other. Instead, they may simply be associated with each other and something else is the real cause.

What is certain is that downzoning takes some development options off the table. Whether that results in an increase or decrease in land prices depends on the property in question, the availability of suitable land for development nearby, and the local demand for lower density housing.

In graduate school, Peddle and his friends would debate whether height restrictions on buildings in Washington, D.C., increased or decreased the value of land. "It's not an unambiguous answer," he says. "You can't develop the land as intensively, so that would tend to decrease the price of land. But it decreases the supply of useable space, which would increase the price."

What's It Good For?

Another way of describing the effect of downzoning is that it alters what real estate appraisers refer to as the "highest and best use" of a property. The Appraisal Institute defines this as the use of land that is "physically possible, appropriately supported, financially feasible, and that results in the highest value."

During his presentation at the April informational meeting on downzoning, Samuels explained to Cecil County residents that there is a point at which downzoning becomes so restrictive that the typical developer isn't willing to pay a higher price than farmers for rural property.

Instead, agricultural land will probably remain agricultural. That would be good news if the landowners can continue to profit from it. Some tobacco farmers, for example, have converted their fields to grow grapes and other high-demand crops. Still, pricing pressures continue to weigh on a variety of agricultural sectors, so farming may not turn out to be the most profitable use of downzoned land.

Someone could purchase the land for low-density development. That would be bad news for local government officials who enacted downzoning to preserve land for agriculture. On the plus side, low-density development doesn't lead to big jumps in population, which require additional roads, utilities, and schools.

Downzoned land could even become a luxury estate. That's not considered welcome news to neighboring landowners. After the April informational meeting, several farmers stood around complaining about downzoning benefiting the rich. The president of the Cecil County Farm Bureau, for instance, expressed his disdain about downzoning resulting in "an increase in affluence."

Why should residents care if downzoning causes upper-income people to move into their community, especially since they make big bucks from the sale of their land? Aside from raising the usual suspicions about the well-to-do, it could make housing less affordable. By reducing the supply of land available for dense residential development, downzoning makes the remaining land more valuable and, thus, more costly for developers acquire. Those costs are, in turn, passed on to consumers. Bottom line: Homebuyers pay more.

In the end, local planners and elected officials must weigh the costs of downzoning against the anticipated benefits. But in order to do that, their constituents have to be informed, and it's easy to get lost in planning jargon and statistical analysis of property value impacts. Halfway through the informational meeting in Cecil County, the slides of scatter graphs caused many eyes to glaze over.

The challenge is to ensure that a community knows what it is getting into with downzoning and why. If they don't perceive downzoning as a worthwhile endeavor for the community and fair to landowners, they'll revolt as they did in Loudoun County, Va., where voters kicked out members of the board of supervisors after they enacted downzoning last year. **RF**

READINGS

Gray, Robert J., et al. *The Effects of Agricultural Zoning on the Value of Farmland*. Washington, D.C.: Resource Management Consultants, Inc., 1991.

Peddle, Michael T. "Farmland Protection Policy: The Effects of Growth Management Policies on Agricultural Land Values." Working Paper CAE/WP 97-7, Center for Agriculture in the Environment, American Farmland Trust, 1997.

Plantinga, Andrew J., Ruben N. Lubowski, and Robert N. Stavins. "The Effects of Potential Land Development on Agricultural Land Prices." Working Paper RWP02-012, Kennedy School of Government, Harvard University, February 27, 2002.

Taylor-Rogers, Sarah, et al. *Downzoning: Does It Protect Working Landscapes and Maintain Equity for the Landowner?* Queenstown, Md.: Maryland Center for Agro-Ecology, Inc., December 2003.

Visit **www.rich.frb.org/pubs/regionfocus** for links to relevant sites.