

COMMONWEALTH OF VIRGINIA



E. M. MILLER, JR.
DIRECTOR

POST OFFICE BOX 3-AG
RICHMOND, VIRGINIA 23208

IN RESPONSE TO
THIS LETTER TELEPHONE
(804) 786-3591
FAX (804) 786-0913

DIVISION OF LEGISLATIVE SERVICES

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DRAFT

TO: Members of the Special Subcommittee Studying Transferable
Development Rights (HB 1187)

FROM: R. J. Austin *RJA*

RE: TRANSFERABLE DEVELOPMENT RIGHTS (TDR)

At your initial meeting you requested a memorandum identifying major issues to consider in addressing whether local governments in Virginia should be authorized to enact TDR ordinances.

The number of articles written about transferable development rights, as someone noted, far exceeds the number of TDR programs which have been adopted. The American Planning Association determined that less than fifty localities across the country had adopted TDR plans as of 1987. Fewer still actually had operating programs. The APA study indicated between twelve and twenty-one localities in which at least one transfer had occurred. Not surprisingly, therefore, analysis of the TDR concept largely has been theoretical and speculative rather than based on broad practical experience.

Transferable development rights programs have been established to promote varied goals. Programs have been adopted to protect historic buildings and landmarks (New York, Chicago, Denver), environmentally sensitive forests and wetlands (New Jersey Pinelands, Collier County, Florida), and to encourage retention of low-income housing. The Montgomery County, Maryland, program to protect agricultural land, cited as one of the most successful programs, is most similar to the TDR uses which have been discussed in Virginia.

This memorandum addresses issues which appear to be relevant to a consideration of state enabling legislation designed to ensure that the interests of individual citizens and the public as a whole are protected, state policies promoted, and the local government not open to unnecessary liability by an ordinance which is legally infirm or suspect. The issues include constitutional and legal concerns, fundamental structural features of a program, and key impacts on the community.

Specifics as to how a TDR program would operate on a day-to-day basis are not included. Virginia Beach and its consultants - the firm of Rogers, Golden and Halpern (RGH) - have responded to these types of questions in the Virginia Beach context. The enclosed documents may be read for purposes of identifying some of these questions:

1. "Questions and Answers About Transferable Development Rights," prepared by RGH for the City of Virginia Beach
2. "Issues Arising Under 'Transferable Development Rights' Programs: A Report for the Transferable Development Rights Subcommittee of the Counties, Cities and Towns Committee of the House of Delegates of the Commonwealth of Virginia (July 21, 1989)

I. CONSTITUTIONAL QUESTIONS

Most legal discussion has focused upon whether TDRs involve a taking of private property and, if so, whether they would constitute just compensation. A few legal scholars have raised additional concerns. Case law has been limited, largely because few TDR ordinances have been adopted nationally and fewer still have actually become operational.

1. Do TDRs Constitute a Taking of Property?

The United States Supreme Court has considered issues raised by development rights transfers in the case of Penn Central Transportation Company v. City of New York, 438 U.S. 104 (1978). TDR proponents point to the Court's majority decision as support for the contention that TDRs do not deprive an owner of all reasonable use of land and thus do not "take" property. Some commentators read the dissenting opinion to indicate that a different decision could result with a different set of facts or with changes in the Court itself since 1978.

The company, owners of Grand Central Station, wished to construct an office building above the terminal. The New York Landmarks Preservation Board, acting under an ordinance designed to preserve historic structures, denied the permit because it would harm the landmark character of the terminal itself. The company would have been allowed to transfer the development rights to several other sites in the area.

The New York Supreme Court held that there had been no taking because the company still had reasonable use of the property, namely continued productive use as a terminal. The Court also noted that the rights could be transferred to numerous sites in the vicinity, several already owned by the company, and at least some of which were suitable for office building development. A majority of the United States Supreme Court agreed with this conclusion. Justice Rehnquist in dissent found that a taking of property had occurred. Key to his argument was a separation of air rights for analysis rather than weighing all rights in the property as the majority had done.

(The New York court's treatment of this case can be contrasted with its finding in a case decided shortly before involving denial of the development of luxury apartments on privately owned park property. In this case, the court found that the transferable development rights were too vague and contingency-ridden to be meaningful. The owners in this case were deprived of any use of the land which would produce a reasonable return.)

2. Do TDRs Mitigate Against the Taking Issue?

As is evident from the discussion above, both the state court and the United States Supreme Court evaluated the nature and value of the transferable right in reaching a conclusion on the taking issue. The Supreme Court observed:

While these rights may well not have constituted 'just compensation' if a 'taking' had occurred, the rights nevertheless undoubtedly mitigate whatever financial burdens the law has imposed on appellants and, for that reason, are to be taken into account in considering the impact of regulation. (at 130)

3. Would TDRs Constitute Compensation for a Taking?

The Supreme Court, having concluded that there was no taking in the Penn Central instance, did not have to confront the compensation issue directly. TDR proponents customarily argue that owners of property whose development is limited do receive "compensation" in the form of the right to sell the development rights and point to the comments of the majority in the Penn Central case, including the quote above, to buttress their position.

Justice Rehnquist in his dissent presented a challenging view. He noted the established rule that just compensation must be not simply an approximate compensation but rather must be a full and perfect equivalent for the property taken. He also raised the question of whether compensation could be other than monetary. Rehnquist would have remanded the case for a determination as to whether the TDRs were such an equivalent, but his discussion of the issue indicated a rather clear inclination to think that they were not.

Summary

Perhaps the best summation of the debate as to the constitutionality of TDRs is that of the American Planning Association, which noted recently that:

(M)andatory TDR programs that impose a zoning or land-use restriction on the protected "sending" sites and create TDRs in exchange may be subject to much closer judicial scrutiny than voluntary TDR programs. The most difficult legal question will be whether the property owner retains any "reasonable or beneficial use or return" from the property after the imposition of the restriction and to what extent the TDRs are an adequate partial or total compensation for the impact of the restriction. The essential question is how far a land-use regulation may go without so burdening a property owner that he becomes entitled to the payment of "just compensation" by the regulator.

The legal doctrines on this point are in fluxIt is not yet clear, however, whether the TDRs in mandatory programs need only be of some economic benefit, or, as Justice Rehnquist argued in dissent in the Penn Central decision, any form of statutory compensation, including TDRs, must not be 'simply an approximate compensation' but must be a 'full and perfect equivalent for the property taken'." (Richard J. Roddewig and Cheryl A. Inghram, Transferable Development Rights Programs: TDRs and the Real Estate Marketplace (American Planning Association: Planning Advisory Service Report Number 401, p. 16, 1987).

While the taking issue has been at the forefront of discussion concerning the legal status of TDRs, it has been suggested that TDRs may be subject to challenge on other constitutional grounds, namely substantive due process violations and abuses of the police power.

4. Are TDRs An Abuse of the Police Power?

A few commentators have raised the possibility that TDRs might be held to involve the "selling" of the police power. (See, for example, Michael D. Strugar, "Transferable Development Rights: Robbing Peter to Pay Paul?" 62 University of Detroit Law Review 633 (1985), who summarizes this and the following argument.) The police power is inalienable, and any attempt to bargain, contract, or sell it away will fail. (Home Bldg. and Loan Assn. v. Blaisdell, 290 U.S. 398 (1933)). The alteration of a police power restriction - a zoning regulation - based upon a party's willingness to pay may be perceived as an abrogation of the police power.

Another potential issue is whether density changes allowed by TDRs redistribute density contrary to zoning policy. It could be argued, so this thesis maintains, that the implication of the TDR-linked density change either is that the density level established by the original zoning was too low and should have been raised by right or that the density level was appropriate and the increased density thus imposes harm.

It should be emphasized that these issues have been raised only theoretically and have not been litigated. TDR proponents generally counter these questions by drawing an analogy to development exactions, such as proffers, where there is a substantial body of law supporting regulations on density allocations and defining the standards which must be met.

II. OTHER LEGAL QUESTIONS

Several other statutory questions have been raised, either in litigation or in general consideration, relating to TDRs.

5. What Authority Exists Under State Law for TDR Ordinances?

Local ordinances nationally by and large have been adopted under home rule provisions or general zoning and land use authority. In Virginia, the Attorney General has issued an official opinion holding that a locality would need specific statutory authority to adopt a TDR ordinance. Such authority could be either by general law or by charter.

6. What is the Relationship of TDRs to the Comprehensive Plan?

The extent to which zoning ordinances and regulations are controlled by the comprehensive plan varies from state to state. In Virginia, zoning must be consistent with the comprehensive plan but the plan serves only as a "guide," not an absolute blueprint, for zoning regulations. Some have questioned whether density transfers through TDRs which exceed comprehensive plan standards might not strengthen challenges that the exercise of the police power was being abused (see #4).

7. Do TDRs Constitute Spot Zoning?

Zoning should provide uniformity of regulation which treats properties similarly situated on an equal basis, and to discriminate in favor of one or a few property owners in a fashion not rationally related to the zoning of the area would constitute spot zoning. The end result of a TDR system is that only some parcels in a receiving zone will actually utilize the increased density from TDRs. Could this result be considered spot zoning? The general response is that all property owners in a TDR receiving area have an equal right to purchase and use the development rights. Whether they do so is a matter of choice, not a produce of the ordinance or decisions by zoning officials.

8. Are TDRs Treated as Securities?

If TDR credits were regarded as securities, they would have to be registered under federal and state law. The process of buying and selling them would have to comply with various reporting requirements and would be much more complicated. In the only litigation on this point, a New Jersey court held that the credits were not a "security" in this sense.

9. Is There a Possible Anti-Trust Violation in a TDR Program?

The issue which has been raised by some commentators is not the TDR concept itself but the possible end result if the local government becomes directly involved as a market player in the buying, holding, and selling of TDRs. In theory, the local government could monopolize the market or, more likely, be of such significant weight that it might be able to favor its own property or TDRs in a transaction, or to favor specific individuals.

III. ISSUES INVOLVING TDR PROGRAM CHARACTERISTICS

A number of practical questions concerning the operation of a TDR program are covered in the attached material from Virginia Beach and its consultant. This section highlights several important policy choices which would determine the nature of a TDR program and affect its effectiveness, acceptance, and impact.

10. Should the TDR Program be Mandatory or Voluntary?

In a mandatory program, the sending area is downzoned or frozen and development thereafter is prohibited. A voluntary program simply gives the property owner the right to sell development rights and accept development limits without affecting development rights of other properties in the area.

The mandatory approach is more likely to succeed if the goal is to ensure the protection of an area as a whole. Based on the limited practical experience with TDRs nationally, indications are that mandatory programs have been necessary if the TDR system is to work.

A voluntary system in theory might be feasible if economic forces were such as to create market demand for rights and induce owners to sell their rights. A voluntary system might also be applicable where the TDR system is also being used as a form of tax assessment relief.

A word of caution is that several commentators feel that the risk of a legal challenge is greater in a mandatory program.

11. Should Development Rights be Transferred in Perpetuity?

The issue is whether the deed restrictions placed on property from which development rights have been sold should run in perpetuity or only for a fixed time period. At some point in the future it may be neither feasible nor desirable to retain in agricultural use land which was so zoned when the ordinance is adopted.

The potential for "windfall" profits and speculative investment if restrictions automatically are to be lifted at the end of a specific period is evident. Yet, the local government may be able to create such "windfall" advantages even if easements are "perpetual" simply by changing zoning densities. A related question thus is whether there should be some fixed period during which the existing level of development rights must be maintained.

The general pattern has been to have the easement run in perpetuity.

12. Should the Local Government be a Party to TDR Transfers?

An issue is whether the marketing of TDRs should be done strictly through the private real estate market or whether the local government should serve as a broker or banker in facilitating the buying and selling of TDRs.

A strictly private system tends to be preferred. A local government, however, might consider a direct role in the TDR program for various reasons. It could do so to create an initial market for sellers and a supply of TDRs for users, establishing trust in the program at the outset. It also could argue that the government can help stabilize the TDR market, guaranteeing a price to the seller in "soft" markets and ensuring a supply of TDRs at reasonable rates when demand might otherwise drive up the price of a limited number of available TDRs.

As noted earlier, direct buying and selling of TDRs might also help head off challenges that the development transfer right benefit or compensation is too uncertain.

On the other hand, at least a few commentators have raised the possibility that a direct banking role for local government might lead to situations which could be challenged as anti-trust violations.

A TDR bank was established in Montgomery County, Maryland. The program itself has been so successful that the bank was never used.

13. Does the Use of TDR Densities Require Special Approval?

An issue is whether a special review process should be established for developments in the receiving zone which will use the acquired TDRs. There may be an inclination to require greater scrutiny of the TDR program and perhaps public pressure from areas in and around the receiving area to do so.

The general recommendation has been that the TDR project be processed as any other, either as a use "by right" or through the normal rezoning or conditional use channels if required by the non-TDR aspects of the project. Building in extra steps, it is argued, will delay the process, cost the developer money, and likely engender resistance by developers to the TDR program.

(See the discussion in Virginia Beach's "Issues Arising Under 'Transferable Development Rights' Programs," 3-5, and also the concerns of developers in this regard reflected in the "Questions and Answers About Transferable Development Rights" paper prepared by the consultants for Virginia Beach.)

Note that a Maryland court held that changes in the sending and receiving zones had to be accomplished through the regular zoning ordinance procedure and could not be left to the discretion of the planning commission.

14. Are Special Procedures Required Before a TDR Ordinance is Adopted?

A TDR ordinance will be required to go through the usual notifications, hearings, and other procedures required of zoning ordinances generally. Given the nature of the TDR concept, however, should any additional procedural safeguards with regard to notification, hearings, findings, and determinations be required before a TDR ordinance can be enacted? The 1989 General Assembly, for example, wrote into the impact fee legislation specific procedures for establishing the basis for, adoption of, and revisions in the imposition of the fees.

15. What is the Relationship of TDRs to Conditional Zoning and Like Techniques?

In a strict sense, there is no automatic linkage. The purchase of TDRs produces the right to increase density. Conditional zoning proffers seek to offset any undesirable effects of density increase. In practical terms, developers are likely to argue for tradeoffs between the purchase of TDRs and conditional zoning and other techniques which are designed to ameliorate the effects of increased density. A developer might buttress this request by arguing that the infrastructure's ability to absorb increased density is implicit in the entire process of establishing receiving zones.

16. Should TDRs be Applied to Commercial as Well as Residential Uses?

The immediate context of the Virginia Beach ordinance appears to be pressure from residential development on agricultural areas. In general, however, development pressures could also be commercial as well as residential. Should receiving areas be established only in residential zones? Should density increases in mixed zones be limited to residential uses? A practical problem is that of how to develop a formula to equate residential density from the sending zone with equivalent commercial development rights in a receiving zone.

IV. ISSUES INVOLVING THE IMPACT OF TDRS

The most difficult questions, given the limited practical experience nationally and the variation in local circumstances which is likely, involve the effects of the TDR program. What effect will TDRs have on conditions in the receiving zones and surrounding areas? What are the likely impacts on property values and taxes? What will be the effect on the availability, cost, and character of housing in the community? The answers largely are speculative. The special subcommittee may want to consider closer examination of the Montgomery County, Maryland, system to determine the TDR impact along these lines in that community.