

Transfer of Development Rights (TDR's) in Florida's Rural Lands (and why they haven't worked)



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The Premise

Transfer of Development Rights (TDR's) programs have been employed for over 20 years in various different locations and applications throughout Florida. The TDR programs in Florida's rural lands are usually driven by the objective of saving a large area of agricultural or environmentally sensitive lands from the impact of future development, or for other environmental virtues, such as water resources or habitat protection. Rural lands TDR programs are typically geared to preserve such lands from premature suburbanization with costly or inadequate infrastructure or from development as 5 to 10 acre "ranchettes". Such forms of development are generally viewed as a form of urban sprawl, which is contrary to the land use policies and goals of state and local planning efforts.

The essence of a rural TDR program is to incentivize the clustering of dwelling units from rural areas that warrant protection to more suitable development locations, either within rural areas or outside rural areas.

These more suitable locations could then be developed in a more compact manner, with less environmental impacts and more efficient delivery of infrastructure. Typically, rural areas in the State of Florida are approved by right for 1 unit per 5 acres to 1 unit per 20 acres, or even less dense for more environmentally sensitive lands. TDR programs usually provide for incentives in the form of "density bonus units" for them to be effective in achieving the clustering objectives. In the majority of the cases, the TDR programs have failed, and have not accomplished the conservation or clustered development objectives.

This paper will show why rural lands TDR programs have historically not worked in Florida, due to market and economic incentives not being sufficient for either a land owner or a developer to transfer and cluster the units to a more suitable development location.

The Mechanics of TDR Programs

Many times, the local governments may really want to achieve their conservation objectives through regulation. But they recognize that in Florida, legal constraints regarding land use regulations could cause such efforts to backfire. Local governments may be liable for compensation to the landowner for taking away private property rights and/or for reducing the land's value.

For a TDR program to work, it must first be market driven. The program will not work if there is no market for the units to be added to the receiving property. Secondly, the TDR program must be economically driven. The value of the sending area must be accounted for, with that land owner being made whole. In fact, it could be argued that the sending area land owner should be made better than whole, if this program is to work on a voluntary and incentive basis. Generally, the rural land owners are not developers, so it is not so much the issue of them utilizing their own property for development. Instead it is an issue of a developer or investor purchasing those TDR's from the sending land owner and then utilizing those TDR's in a clustered development format on designated receiving lands.

In the analysis included with this paper, it is assumed that a developer would purchase the TDR units from the sending land owner at a price that has a suitable relationship with the price of a finished home within a compact development. **Figure A shows the relationship between finished home value, finished lot value, and raw land price.** Keep in mind the raw land unit price, sometimes referred to as the "unit blank" price, includes the value of the underlying land upon which the property will be developed, as well as any TDR costs that must be acquired for the residential land units. In other words, the TDR cost is really a part of the land cost allocation. TDR's should not be considered as a development or building cost element since those costs

must also be within market norms. Further, it would not be appropriate for the cost of TDR's to come out of builder or developer profits, since that must be maintained for an entity to even be in the development business, especially considering its associated risk.

Assuming a developer purchases the receiving land for development of a compact subdivision, the receiving land value must be accounted for in the land cost of the units. So, a developer must purchase and hold the receiving land, or option it in some fashion, until he/she has sufficient TDR's tied up or purchased from sending

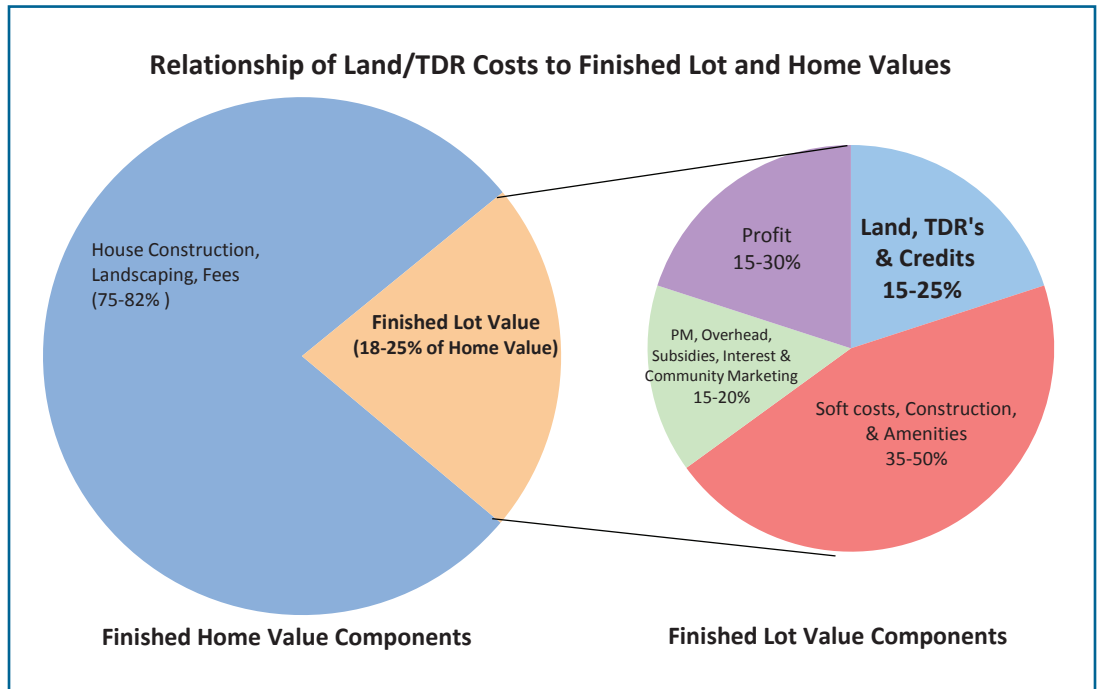
areas to develop the desired compact subdivision. The developer has to amortize both costs into the developed units, i.e. the underlying receiving land costs as well as the TDR costs.

When a developer purchases TDR's, there must be an accounting for the time value of his/her money and the transactional costs, recognizing that many times there can be several years between the time of the purchase of TDR's and the actual utilization of the TDR's in the developed receiving lands. This could be anywhere from 2 to 5 years depending on the entitlement program and the market. If the sending land owner is not willing to hold a mortgage or some type of longer term option arrangement on those TDR's, then the carry cost to the developer must be accounted for, and the TDR price must be discounted accordingly.

OK, then what does it take for TDR's to work?

Now, the bottom line on how TDR programs must be structured in order to work. **There must be a unit bonus multiplier applied to either the sending and/or the receiving land areas which provides sufficient equity to both sides.** It is in setting this bonus multiplier where

▶ **Figure A**



the public officials generally come up short. In fact, some of the multipliers required can seem excessive and public officials may be concerned that there is a “windfall profit” for someone. Both the sending and receiving areas must benefit from the TDR program, or come out at least whole, if the TDR program is to work. That is not to say the TDR program should create a windfall for either side but again, this is a program that is based on incentives, and TDR programs are generally voluntary for land owners.

Attached Figure B shows an example of what TDR multipliers would be required based on reasonable assumptions for end home value, the relationship to the underlying land value, what the developer can pay for a TDR and what the sending area land owner must receive for adequate compensation. It is clear that the value of the underlying sending and receiving land can greatly affect the multiplier required. The bottom line of why TDR's generally do not work is - they require a bonus multiplier of 5, 10, 20 or more times the number of units allowed by right in the sending or receiving area for the economics to work. Public officials are often reluctant to accept these multipliers as necessary.

Another variable which affects the TDR multiplier is the underlying density of the sending area. If it is very low - say 1 unit per 10 to 20 acres, then a higher multiplier will generally be required to make the sending land owner whole, and to allow the receiving land owner or developer to purchase the TDR's at a price that works for land development feasibility.

It can generally be found that, **in areas where TDR's have been declared a success, the home values for the market area are relatively high end.** Those higher home values can absorb higher land and TDR unit costs. The problem in the future will be that home prices will likely be more moderate for many years ahead, versus what was seen in the mid-1990's to the mid-2000's. In areas where a TDR program may have worked for a period of time in the past, especially where the market was hot and the prices were

high and escalating rapidly, TDR programs may not work in those same areas going forward.

Other Issues to Ponder

The **underlying value of the receiving area** must be accounted for in the calculation of the developer's costs. This has been a major fallacy in many of the TDR analyses, in that the analyst may consider the price of the TDR as a land unit cost, but disregard the fact that the TDR costs are being placed on land that also has value and must be amortized into the cost of the developed units. That underlying value isn't just allocated to the by-right units on the receiving land, but needs to be added to the cost of the TDR's to calculate the total land cost, and then divided by the total units to be developed, to come up with an average land cost per unit.

Non-residential uses, i.e. commercial, should be allowed by right, without purchase of TDR's, at least up to an amount that services the residential compact development. Over that amount, TDR's purchased for commercial properties, just as with residential, must be in reasonable proportion to the land value added, based on market factors.

Requiring clustering of units without bonus incentives is sometimes thought of as a break-even scenario by the public officials, but this is far from the case. Low density units have a much higher value on a per land unit basis, say as a five acre or ten acre tract, than would a compact land unit at 3 units per acre (e.g. 1/4 acre lots), which must then be developed into an urban-type subdivision with

► **Figure B**

TDR ANALYSIS for AGRICULTURALLY ZONED LANDS		9/12/2010	
Scenario 1 - Base Density at 1unit/10 acres		Scenario 2 - Base Density at 1 unit/5 acres	
Underlying Land at \$10,000/acre		Underlying Land at \$20,000/acre	
Sending Lands			
Assumed acres	1,000	Assumed acres	1,000
Approved Density per acre	0.10	Approved Density per Acre	0.20
Approved Units	100	Approved Units	200
Assumed Land value per acre	\$10,000	Assumed Land value per acre	\$20,000
Base Land value	\$10,000,000	Base Land value	\$20,000,000
Assumed value of remaining Ag per acre	\$5,000	Assumed value of remaining Ag per acre	\$5,000
Value of remaining Ag land	\$5,000,000	Value of remaining Ag land	\$5,000,000
Value of transferred units	\$5,000,000	Value of transferred units	\$15,000,000
Value of one transferred unit	<u>\$50,000</u>	Value of one transferred unit	<u>\$75,000</u>
Receiving Lands			
Clustered village density	3.0 du / acre	Clustered village density	3.0 du / acre
End user price (house and lot)	\$250,000	End user price (house and lot)	\$250,000
Lot to Home Value ratio	20%	Lot to Home Value ratio	20%
Finished Lot Price	\$50,000	Finished Lot Price	\$50,000
Raw Land % of Finished Lot	20%	Raw Land % of Finished Lot	20%
Raw Land per unit (blank)	\$10,000	Raw Land per unit (blank)	\$10,000
Assumed Number of Units	300	Assumed Number of Units	300
Amount Developer can pay for 300 units	\$ 3,000,000	Amount Developer can pay for 300 units	\$3,000,000
Acres of Underlying Receiving Land	100	Acres of Underlying Receiving Land	100
Value per acre of underlying land	\$ 10,000	Value per acre of underlying land	\$ 20,000
Underlying Land Value of Receiving Area	\$ 1,000,000	Underlying Land Value of Receiving Area	\$ 2,000,000
Additional Units from Underlying Land	10	Additional Units from Underlying Land	20
TDR's needed for 300 units	290	TDR's needed for 300 units	280
Amount Developer can pay for TDR's	\$ 2,000,000	Amount Developer can pay for TDR's	\$1,000,000
Amount Developer Can Pay for Each TDR	<u>\$6,897</u>	Amount Developer Can Pay for Each TDR	<u>\$3,571</u>
Density Bonus Multiplier Required	<u>7</u>	Density Bonus Multiplier Required	<u>21</u>

Note: This analysis assumes that a developer would purchase land within a receiving zone of an agricultural area and purchase sufficient TDR's to create a 300-unit single family development on 100 acres. It also assumes that the land value of the remaining underlying agricultural use of the sending land would be \$5,000/acre. The resultant multiplier required would be in the form of a density bonus, either on the sending area and/or the receiving area.

related infrastructure. For example a 5 acre lot may have a value of \$50,000 without infrastructure, whereas a small lot in a developed subdivision could have a \$50,000 value, but is burdened with the cost of full infrastructure. Thus, clustering of units without bonus unit incentives can result in significant land devaluation to the underlying land owner.

Even though clustering of units without any increase of density or bonus units is not an equitable solution, TDR's with appropriate bonus unit incentives generally do work well for **internal shifts within a single ownership property**. In this situation, there is no carry cost of the TDR units, no transactional costs and no acquisition fees. The underlying land owner owns both the sending and receiving lands, and can cluster the units and receive the additional bonus densities. This assumes there are sufficient sending areas that the land owner owns as well as appropriate receiving areas. Then, the land owner could sell that approved compact village directly to a developer, essentially as development-ready. This way, the developer is able to pay more for the land and the units, and the rural land owner receives more value for his/her property. The risk is that many times the conservation easements placed onto the sending lands that restrict development cannot be undone if the land owner later decides that he/she doesn't care to continue under the TDR program.

Another issue is that, many times, the public officials prefer that the **TDR units be transferred into existing urban areas from rural areas**. The problem with this strategy is that generally those urban areas already have sufficient density by right, based on comprehensive plans that encourage dense development in the urban areas. Certainly, if the local government wants to encourage the higher dense development in the urban areas, it is difficult to do that by adding costs to achieve those additional densities. A TDR program generally works best in areas

that need the density and where the market will pay for the density. This would include communities, villages and new towns in appropriate locations in rural areas, accomplished by clustering of the TDR units.

The addition of residential units created by the TDR bonus units presents somewhat of a political dilemma for public officials, in that it **places more population in the rural area**, which raises the issue in Florida of "**Basis of Need**" for the additional units generated by this incentivized program. Under current planning policy administered by the State, there would have to be justification for the additional population accommodated by the TDR program with these additional bonus units. The local government generally would not want to take away from the population of the dense urban areas to create this TDR program, so from a population perspective, there would have to be a net increase of the projected future population in the overall local jurisdiction, within the planning horizon of the comprehensive plan. In recent years, that has been a tough issue to justify to state planning officials.

Wrap Up

In conclusion, the TDR program must be market and economic driven for it to work, not regulatory driven. The value of the TDR must have the right relationship to the value of the underlying sending land, to the value of the receiving land, and to the value of the finished compact residential product to be developed on the receiving land. For TDR's to work, they require appropriate and sufficiently high bonus density multipliers, which can present regulatory and political dilemmas. At the end of the day, there must be a market for the end residential or mixed use product in order for any TDR program to work, and an incentive for the rural land owners to participate.



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