

To: Mayor Muriel Bowser
From: Tomi Dapshi, Margaret McLaughlin, and Mary Stottele
Date: March 23, 2016
Re: Proposal for D.C. Municipal Land Bank

Introduction

Over the past 40 years, states and municipalities across the United States have developed land banks in order to spur development of blighted and abandoned properties. Washington D.C. with its notoriously slow policymaking process is one of the last few cities without an authority that addresses these issues. We recommend that Washington D.C. institute a land bank to responsibly develop blighted and vacant properties and return them to tax-paying status. We begin with an overview of land bank use, go on to explore the current land use environment of Washington D.C., and conclude with our specific recommendations and their potential effects.

Land Bank Basics

Land banks are publicly owned entities designed to acquire, manage, and develop properties that are foreclosed, abandoned, or blighted. Relatively new tools, their use has seen a significant uptick since the 2008 housing crisis that left many local governments with large quantities of foreclosed properties. As these types of properties begin to accrue in communities, they create negative externalities, such as increases in illicit behavior, both for neighboring properties and for the local governments in which the properties are situated. A reputable study from Temple University found that all else equal, an abandoned house on a block reduces the value of the other properties by an average of \$6,720.¹ Costs to governments associated with foreclosed properties include increased use of police in these neighborhoods, increased reliance on fire emergency personnel due to increased arson and accidental fires in abandoned property, and increases in the use of municipal services for foreclosure procedures.²

Developing a land bank system allows for municipalities to reinvent the way that they move foreclosed and abandoned properties to resale. In the standard system, local governments sell or auction tax liens in order to earn a discounted profit and to quickly advance the resale. The creation of a land bank authority consolidates this process and allows for a more strategic and longer-term vision of property use across the entire city or metropolitan region. Additionally, most land banks incentivize purchase of otherwise unviable properties in the private market by forgoing the collection of back taxes.

¹ <https://astro.temple.edu/~ashlay/blight.pdf>

² <http://www.communityprogress.net/filebin/LandBanksLandBankingVer2DigitalFinal.pdf>

Land Use in the District of Columbia

Although Washington, D.C. has a notoriously competitive property market, there is still significant blight in some areas of the city. Roughly 1,300 parcels of land are considered blighted or vacant by official governmental tallies.³ Additionally, property inspectors are not able to keep up with the number of reported vacant properties due to the burden of bi-annual check-ins on the progress on existing blighted properties. That in conjunction with the fact that the city only has four property tax assessors makes it quite likely that the number of vacant properties is actually larger than 1,300. Currently, councilperson at-large Elissa Silverman is working with the Department of Consumer and Regulatory Affairs to shift the burden of bi-annual check-ins from the city to the property owner. Property owners would be responsible for providing proof of improvement or occupancy of previously blighted properties in order to be removed from the blighted or vacant property lists.⁴ This would allow more frequent and accurate assessments of the D.C. vacant and blighted property registry.

Washington takes measures to incentivize homeowners either to repair their blighted homes or to sell to someone who can. The normal residential property tax on residences in the District is 0.85% on the assessed value of the property. A property that is designated vacant by one of the city's assessors is subject to a 5% tax. The rate doubles for properties assessed to be blighted⁵; however, there has been evidence that developers make use of a loophole, wherein they obtain a construction permit from the city, but never begin the work on repairing the structure and thereby avoid the tax penalty without rectifying the issue.⁶

Washington D.C. currently encourages reuse of vacant, abandoned, and blighted properties through the Property Acquisition and Disposition Division (PADD) in the Department of Housing and Community Development (DHCD). The department is charged with a mission similar to that of a land bank, but it lacks the nimble structure that a land bank provides as an independent authority. PADD's three functions are to help homeowners fix homes that are in disrepair, to acquire properties through various means, and to dispose of properties through sale to developers or individuals who will then convert them into either affordable or market-rate housing. PADD disposes of property through lottery, auction, or a request for offers on the property.⁷

D.C. Land Bank Proposal

³ <http://dcra.dc.gov/publication/blight-and-vacant-buildings-list>

⁴

http://www.elissasilverman.com/councilmember_silverman_introduces_bill_to_strengthen_enforcement_on_vacant_properties_in_district

⁵ <http://otr.cfo.dc.gov/page/otr-vacant-real-property>

⁶

http://wamu.org/programs/metro_connection/15/10/09/why_does_dc_have_so_many_vacant_houses_when_real_estate_is_so_pricey

⁷ <http://dhcd.dc.gov/service/property-acquisition-and-disposition>

We propose that the municipality of D.C. convert the eyesore of vacant and blighted property into an asset through the creation of a municipal land bank. We recommend dissolving the Department of Housing and Community Development's (DHCD) Property Acquisition and Disposition Division (PADD) and establishing a full-fledged D.C. Land Bank.

Structure

We recommend that the land bank be established as both a public authority and a non-profit, headed by a Board of Advisors that incorporates the DHCD, housing and planning nonprofits, political appointees, and industry stakeholders. Nonprofit status will allow the land bank more flexibility in applying for funding and in creating partnerships, while public authority status will imbue the organization with powers to regulate and maintain public property.

In addition to the Board of Advisors, we recommend that the land bank incorporate a Citizen Advisory Board that represents a wide variety of neighborhoods and backgrounds. These citizen-advisors will serve as neighborhood ambassadors for the land bank. They will monitor and guide the creation of land bank policy in conjunction with the Board of Advisors. Most importantly, they will have sales procedure review and be responsible for reviewing and approving applications for purchase and sale of land bank properties. We recommend that DHCD partner with the Coalition for Nonprofit Housing and Economic Development (CNHED) in the search for Citizen Advisory Board Members. The CNEHD is an organization that already has deep ties within the D.C. housing community and boasts over 140 grassroots partner organizations.

Property Identification and Classification

The land bank will obtain a list of currently registered vacant and blighted properties from the Department of Consumer and Regulatory Affairs' (DCRA) Vacant Building Enforcement (VBE) unit. The land bank will work with property assessors to identify all future vacant or blighted properties. In coordination with the VBE, the land bank will develop a classification system for vacant and blighted properties based on the extent of repair required to bring the property up to code. For example, the land bank could rank properties on a 1-5 scale with 5's assigned to properties earmarked for demolition and 1's assigned to properties that need relatively minor repairs.

Acquisition of properties

All currently seized property should be transferred from the DHCD PADD to the land bank upon its establishment. Future property acquisition will follow a detailed legal process. The first step will be notification of foreclosure on tax delinquent property. To address concerns of displacement, the land bank will work in conjunction with the DHCD's Housing Counseling Services to develop foreclosure prevention training. A similar strategy was employed in Greater Syracuse Land Bank,

and 74.9% of owner-occupants have avoided foreclosure, primarily by entering into back tax payment plans.⁸

The land bank will face a choice with each property that is abandoned, vacant, or blighted: to buy or not to buy. In the District, this could depend in part on whether taxes are being collected at an increased rate for vacant or blighted properties. This may require auditing the history of tax payment on the property. The economically efficient decision will be to choose the option with the lowest present value of total costs. The discount rate should take into account the risk associated with the property, which is associated with both the perceived future price of the parcel as well as the timing of when developers would demand the property.⁹ Foreclosed properties will be transferred to the land bank. In order to remove barriers to purchasing foreclosed properties, all back property taxes on foreclosed properties will be forgiven once acquired by the land bank.

Sale of land bank properties

We recommend an open and transparent sale process for all land bank properties. All for-sale properties will be clearly listed on the land bank website along with any outstanding code violations or necessary repair work. The Land Bank's Transaction Supervisor will determine the sale price for a property. To determine the price, the Transaction Supervisor will start with the assessed value, add the cost of any upkeep that the Land Bank has put into the property, and adjust for the recent sale price of surrounding properties. Additionally, if the property will require considerable work to be brought up to code, the Transaction Supervisor will lower the purchase price.

Applications will be open to all. The Citizen Advisory Board will review all applications for purchase, and will prioritize sale to those living within the community or to those with ties to the community in order to avoid a pattern of delinquent ownership from out-of-town LLC's and other low-end speculators. Any party wishing to acquire a land bank property must be able to demonstrate ability to pay in full upon time of sale.

With regard to selling strategy, we recommend that the land bank prioritize sale of relatively good quality and higher market-value properties in order to create a fund reservoir to balance future losses for demolition of unsalvageable property. We also recommend that the land bank reserve the right to hold and bundle properties concentrated in the same area in order to make large sales to developers as an investment product, thereby improving neighborhoods on the whole instead of one property at a time.¹⁰

⁸ Metropolitan Government and Politics lecture, March 8, 2016, by Paul Driscoll and Stephanie Pasquale, City of Syracuse Department of Neighborhood and Business Development

⁹ <http://onlinelibrary.wiley.com/doi/10.1111/1540-5850.01113/epdf>

¹⁰ http://www.thelandbank.org/downloads/Land_Bank_Related_Questions.pdf

Property taxes on sold properties

In addition to forgiveness of back property taxes, we recommend two optional property tax proposals for sold land bank property. The Advisory Board may choose one or none, depending on the market value and demand for a particular property:

(1) To recognize the land bank's impact on future increased property tax revenues, we recommend that 50% of the property tax from sold properties be earmarked for land bank funding for 5 years after transfer of property from the land bank to a private owner. This model has been followed by the Michigan land bank.¹¹ The use of this option ensures continued funding of the land bank and allows it to continue to pay high demolition and upkeep costs that the city no longer incurs. Additionally, since the legal ownership of abandoned and blighted properties insulates the city from legal action, the city would be likely to agree to forgo a small portion of its tax revenue from certain properties.

(2) Alternatively, to incentivize private ownership, we recommend property tax abatement for five years after transfer of property from the land bank to a private owner. This model has also been used by the Michigan land bank.¹² This option would be reserved for houses that require a considerable amount of work in order to be brought up to code. It may also be used in rare circumstances to incentivize first-home ownership in struggling communities.

¹¹ <http://www.umich.edu/~econdev/landbank/>

¹² Ibid.

Implications

Community Impact

Blighted and vacant properties are associated with a variety of urban issues including, but not limited to, higher crime rates, lower property values, decreased government revenue, and overall stunted quality of life for those left in blighted neighborhoods. Returning such properties to productive use alleviates urban blight faced by those living near the properties by reducing the above-mentioned negative externalities. Additionally, resulting increases in the tax-base for a given area go toward improving government service levels.

Efficiency

Whenever government intervenes in any market (especially housing), it introduces distortions to the marketplace. Since the land bank program involves a high level of government intervention, it would indeed create market distortions; however, since the presence of vacant properties is considered a market failure, government intervention is warranted. The issue for the land bank is whether the distortions created by government intervention are offset by the benefits to the community that the program provides. Some argue that the land banks are not economically sustainable because the operational costs may exceed the revenue gained from selling properties; however, any cost-benefit analysis of a land bank should include the social costs of leaving land vacant and the long-term benefits of new tax-productive land in addition to the real costs and benefits.

Elimination of back taxes and tax breaks incentivize purchase of vacant land

If left to the devices of the private market, many vacant properties would likely not sell due to both large tax liens and poor condition. Such properties would continue to deteriorate, leading to decreased valuations for the surrounding properties and potentially creating more vacant properties. By choosing to forego the city's claim on back taxes, land banks can purchase and sell properties that would not be viable in the private marketplace. This is a huge advantage over the current system, which requires purchasers of seized property to pay all back taxes. Additionally, by prioritizing the sale of relatively high quality properties early in the land bank's creation, the land bank can subsidize the sale of worse properties to responsible parties for their renovation and reinvestment in the community.

Additionally, the land bank can incentivize purchase of a particularly undesirable property through tax abatement. This lowers the present value of the property, which can impact the decision-making process of the purchaser and incentivize future investment.

Land banks have more flexible revenue-raising capacity

Land banks are also more efficient than the current DHCD entity because of their quasi-governmental status. Because of this, they are eligible for funding streams such as private and nonprofit grants and federal subsidies that a government agency would not be able to apply for. These additional funds can further subsidize the sale of undesirable property or be used to demolish completely unsalvageable properties.

Land banks reduce low-end speculation

If administered irresponsibly, the land bank runs the risk of turning into a mechanism for property owners to irresponsibly “flip” property, that is buying housing cheaply and then renting those houses out without consideration of adequate living conditions. It would be a boon for low-end speculators; however, our proposal mitigates this risk with three elements: eliminating auctions, giving jurisdiction on sales decisions to community ambassadors, and allowing properties to sit tax free for as long as the land bank holds the title. In the current auction system, vacant and blighted properties are sold to the highest bidder, which oftentimes is an LLC or slumlord that has very little interest in re-establishing the property beyond fixing basic code violations. By eliminating the auction, the land bank can be more judicious in deciding who obtains properties. In the same vein, giving approval of sale to the Citizen Advisory Board, which has eyes and ears in the community and prioritizes community members, will reduce the likelihood that a property will fall into the hands of a known slumlord or irresponsible property developer. Lastly, once a property is acquired by the land bank, it is held tax-free until time of sale. This eliminates pressure to sell properties quickly, allowing the land bank the time to find responsible owners or developers.

Land banks harness the neighborhood effect through bundling

Bundling properties is an extremely efficient means of harnessing the neighborhood effect, wherein the property values of an entire neighborhood are increased by the development of a significant number of nearby properties. Additionally, the improvements made to an area via bundling are more sustainable than those gained by randomly improving a single property in a blighted area. Bundling also provides a means of unloading particularly undesirable properties that may never have been sold otherwise by including them in a package with either more desirable properties or more land. This minimizes the risk of taking on such properties on the investor and incentivizes holistic improvement of a larger area. These larger-sized bundles are also more attractive to mixed-use developers that can bring commercial and economic development to a previously run-down area. Bundling in conjunction with the application process will allow for the city to develop a longer-term vision of neighborhood development.

Equity

Introduces horizontal inequity

Forgiveness of back taxes and various tax abatement programs within the land bank introduce horizontal inequities between owners of land bank and private properties of the same value; however, we argue that land bank owners merit such preferential treatment in the short-term because they have committed to putting in their own time and resources to turn around a property and bring it up to code, which in turn provides positive externalities for the entire neighborhood.

Gentrification

The larger equity issue with land banks is that of possible gentrification. If the land bank program works as expected, then one would expect the values of surrounding properties to increase. Since most abandoned properties are located in low-income areas, this may pose a burden for homeowners, who will see an increase in their property tax levy. A certain percentage of residents may not be able to afford to remain in their neighborhood; however, there are two factors that mitigate this. First, the number of people who would be adversely affected by the land bank program pales in comparison to the amount of people who would benefit. Since low-income communities are disproportionately affected by abandoned properties, renovating these properties is an essential step in increasing the economic prosperity of these neighborhoods. Second, the homeowners who face a larger property tax burden will be able to capitalize on their increased home equity by either selling the property or borrowing against the new equity.

Foreclosure assistance

Another important equity consideration is the impact of foreclosure on low-income owner-occupants. Our recommended foreclosure-counseling course will work to abate this effect. Additionally, we recommend that the land bank work in conjunction with the D.C. Department of Human Services and the Coalition for Nonprofit Housing and Economic Development to connect owner-occupants to possible federal programs and housing assistance.

Conclusion

The main objective of the land bank proposal is to return vacant and blighted properties to productive use. In order for the land bank to be successful in meeting its objective, it has to be cost-effective, sustainable, and beneficial. Through the sale of land bank property, earmarked taxes, and federal and private grants, the proposed land bank will generate enough revenue for itself in the long-run to provide the necessary funds for operations and services. Additionally, through judicious buyer approval processes and bundling, the land bank will contribute to the sustainability of neighborhood reforms. Finally, the land bank will be beneficial to all residents of blighted areas. Returning vacant properties to productive use not only has impacts on crime and morale, but also expands the property tax base, thereby increasing revenue for the Washington D.C. government, which can be reinvested in better services for low-income communities. Overall, this proposal puts D.C. residents in more favorable housing situations and provides D.C. with the groundwork for increased economic development.