Using Impact Fees to Finance Schools and Other Public Construction Occasioned by New Development

Presentation to:

Omaha Together One Community
Metro Area Development Committee

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Outline of Presentation

- Fiscal consequences of new residential development: Capital costs (land, buildings, equipment) of new or expanded public schools, fire stations, arterial roads, parks, trails, water and sewer treatment plants and lines.
- Who should pay for these capital expenditures: All taxpayers in the jurisdiction (city, county, school district), the property's developers or builders, the residents and/or businesses occupying the development, or some combination of these sources of funds?
- Traits of equitable development impact fees
- Questions for discussion about the possible adoption or rejection of impact fees

Population Growth:
1990-2000
Omaha grew by 16.2%, the Omaha Metro Area, by 12.1%
Lincoln by 17.5%

The Costs of New Schools

The Costs of Constructing New Schools Depend on:

- Need for new student seats, which in turn depends on:
  - The numbers of public school students likely to come from the new homes and their distribution across the three levels (elementary, middle, and high school)*
  - The number of unused classroom seats remaining in existing school buildings that are within acceptable busing distances of the new development.
- Land and building costs per student seat

Fiscal impact fees typically fund only "capital expenditures," i.e., for land acquisition, construction, and purchase of equipment of at least one year's "life expectancy." These fees are not supposed to be used for salaries, electricity, supplies, and other consumables.

*Base forecasting of average number of students per new home on local inventories of the same kinds of homes (e.g., detached single-family for first-time buyers, trade-up homes, town-homes for retirees) as those likely to be built for your community or the sections of your community under analysis; beware of regionally derived averages that are inappropriate to your community.

Average Costs Data from 110 New Schools Completed or Under Construction, 2001 and 2002 in Nebraska, Kansas, Missouri, and Iowa

Level of School	Cost per student	Cost per sq. foot	Median number of students
Elementary	$11,176	$103.48	600
Middle	$15,765	$94.39	575
High	$12,222	$91.67	900

Two Examples of Forecasting Public Students Likely to Come from New Single-Family Homes: Using Recent-past Enrollments as Best Guides to Near-future Demand for Classroom Seats

Level of School	Tahoma District, Washington	Windham District, New Hampshire
Elementary	.516 students on average	.311
Middle School	.181	.113
High School	.146	.103

Estimated Elementary School Students and Construction Costs, Given Three Residential Development Scenarios (i.e., average number of dwelling units [DUs] per acre) for a Square Mile of Farmland (640 acres)

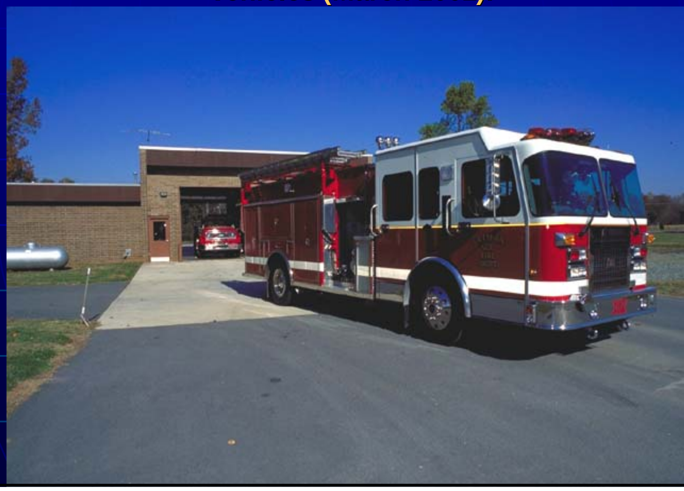
(1) Density Scenario	(2) Number of dwelling units (DU) in a mile square at that density	(3) Estimated Elementary school children per DU	(4) Estimated Total Elementary Students (2) X (3)	(5) Total estimated building costs (4) X $11,176
Suburban (3.4 DUs per acre)	640 X .9 X (buildable space) X 3.4= 1,958	.311	609	$6.8 million
Suburban/ Urban (5 DUs pa)	2,880	.311	896	$10.0 million
Urban (7 DUs per acre)	4,032	.311	1,254	$14 million

Construction Costs Associated with a Square Mile of New Development

- According to Omaha's Planning Department, the City has been approving subdivision plats covering in the aggregate about 1.5 square miles of new development per year.
- As the previous slide indicates, unless there are many vacant seats in existing schools within reasonable busing distance of the new developments, one or more new elementary schools would be needed to serve the single-family homes built within that square mile (assuming about 600 seats per new school).
- The arterial roads (i.e., on the edges of the square mile) may need upgrading from rural standards.
- Also needed to serve this square mile will likely be extensions of water mains, sanitary sewers and storm sewers.
- And that square mile, along with several others, may need a new fire station, vehicles, and equipment (as well as additional police cruisers, among other types of service equipment).

As this area builds out, traffic volumes may occasion the need for an extra lane or two (as well as broader shoulders) on the arterial roads, at a possible cost of several hundred thousand dollars per mile.

If response times are to be kept to reasonable levels (e.g., within 4 minutes for heart-attack victims; 7 minutes for fires), a new station with equipment may be needed (probably for several square miles of development rather than just one). A new station in San Mateo, CA, accommodating 3 fire-fighters and a battalion chief, one engine and one ambulance cost about $2 million, not counting the vehicles (March 2002).



Who should pay for the public construction and equipment costs caused by new development?

- All taxpayers in the same jurisdiction (e.g., school district, municipality, county)?
- The developers of the property?
- The residents (or business occupants) of the property?
- Some combination of the above potential funding sources?

What stakes does the community as a whole have in the provision of adequate services for new residential developments, and are those stakes sufficient to justify having all taxpayers foot the whole bill for the services?

- Schools: If the new developments in a square mile did not have their own schools?
- If they went without their own parks and biking/walking trails?
- No public water and sewer lines: If the new homes in a square mile were compelled to have their own water wells and septic fields?
- The adjacent arterial roads (often the "section-line" roads) were not upgraded?

What stakes do the developers have in the provision of adequate public services to their properties?

- Too difficult to sell suburban-density home sites (around 3.4 dwellings per acre) if the adjacent county road remains unpaved? Examples in Douglas County of developers widening county roads at their own expense.
- Anecdote from Douglas County: Developer approached the school district and said words to the effect, "I can't convince people to buy here unless you build a primary school here."
- Without either public sewers or a package sewage treatment system provided by the developer, suburban-or urban-density lots are not possible. Instead, each home may be required to have as many as three acres (i.e., to accommodate a septic field).
- Developer may be able to pass all or most of the capital costs of the provided services on to the home buyers. The sale prices are higher, or the new residents are assessed special taxes or other fees to cover the payments of principal and interest that go from the home-owners' association to lenders.

What stakes do residents of the new development have in the provision of adequate schools, roads, parks, sewer and water lines, etc.?

- Their homes' values tend to go up with the quality of those services. An elementary school within walking distance, city water supplies, good roads leading to town or the interstate, a subdivision park, and other public facilities should all add value.
- Evidence of residents' willingness to pay for them: In Colorado, Nebraska, and other states, special jurisdictions called "sanitary sewer improvement districts" (or SIDs) are established under state law, with the approval of the county legislature. One created in Mesa County, Colorado, in June 2001 was proposed by petition from nine owners who agreed to be assessed $4,435 each to cover the costs incurred by a public sewage treatment system, in addition to $750 each in a "Plant Investment Fee" and $1,000 to $1,750 in a "Trunk Line Extension Fee," "depending on the lot size."
- These assessments may be paid in installments to cover bonds. If so, and a city annexes the SID before the bonds are paid for, it (the city) assumes the debt burden. That is, all taxpayers in the city become responsible for bond payments of principal and interest.

The Pros and Cons of Impact Fees

- **Pros:**
  - The direct beneficiaries pay a "proportionate share" of the capital costs of servicing their homes, i.e., some share that is higher than what house-holds in other parts of the city or school district are taxed to help pay for those facilities.
  - Jurisdictions (cities, county governments, school districts) that are already stretched fiscally have an additional source of funding for infrastructure (albeit only or mostly for facilities in the newly developed areas).
  - "Slow-growth" movements will not have the argument that new developments are fiscally ruinous.
- **Cons:**
  - Builders will pass fees' costs on to consumers, denying some or many buyers the homes that they could otherwise afford.
  - Fees for middle-class homes may be excessive relative to those homes' actual fiscal impacts.
  - Upscale homes may already generate enough tax money to cover the capital costs of servicing them.
  - Rival communities that don't have such fees will out-compete ours for new construction.
  - State law may not permit impact fees, either imposed by a city or by a school district.

Impact Fees May be Designed to Avoid or Minimize Their Potential Negative Consequences:

Examples from Phoenix, AZ, and Lincoln, NE

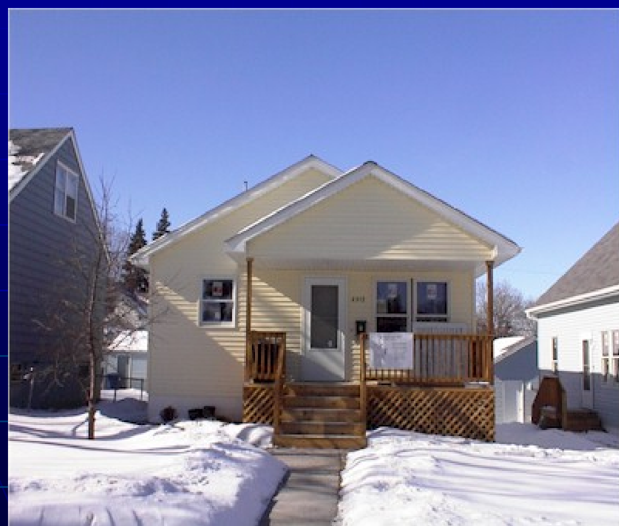
- **Problem**: Deserving potential buyers cannot afford the homes they want because developers add the fees' costs to the sale price.
- **Solution**: *Keep fees as low as possible.*
  - Phoenix's ordinance divides the city into (1) "feeless" areas where existing public facilities are largely sufficient to meet the needs of the expected new development and

    (2) "seventeen impact fees areas."
  - The fees vary by the adequacy of service facilities in place in each area, i.e., the more adequate, the lower the new investments required and the lower the fees. As of July 2003, those fees ranged from $1,868 per "standard single-family home" in one of the 17 districts to $10,354 in another. The total "Net Development Impact Fee" consisted of separate contributions for fire protection, libraries, "major streets," parks, police, solid waste, storm drainage, wastewater, water, and "Equipment repair."
  - It was a "net fee" because deducted from the estimated full capital costs of servicing new developments per fee area are estimated "revenues that future development will contribute to infrastructure funding": water and sewer rates allocated to capital facilities, sales taxes earmarked for infrastructure, property taxes assigned to pay off bond principal and interest, etc.

Traits of Equitable Impact Fees: 1--Exemptions

- Homes designed for moderate- and low-income households may be completely or partially exempted from impact fees.
  - Lincoln's January 2003 impact fee ordinance (No. 18113) provides for a 100% exemption to owner-occupied new homes where the household earns 60% or less than the area's median gross income adjusted for household size *AND* the home is located in an "Income Area, Low. An area where 50% or more of the households within a census block make 60% or less of the median gross income adjusted for household size."
  - It provides for a 50% exemption for households earning more than 60% up to 80% of the median *AND* where the home is located in an "Income Area, Moderate. An area where 50% of more of the households . . . make 80% or less of the . . . ."
  - Fees may be waived or reduced also for individual homes in other areas that are rented to low- or moderate-income families (as defined above).

Home Built by Habitat for Humanity in the Twin Cities, Minnesota, Area



Consequences of Development Impact Fees for Middle-Class Home Buyers

- **Affordability for the buyer:**
  - According to US Census Bureau, the median household income in Douglas County in 1999 was $43,209.
  - Let's say that by 2003 it has risen to $48,000 or $4,000 per month. Let's say also that the banks allow us to incur home-ownership debt of 28% of our gross monthly income; 28% of $4,000 is $1,120.
  - Let's say that taxes and insurance amount to $300 a month, leaving $820 to spend on the mortgage.
  - With a 6 percent interest rate for a 30-year fixed mortgage, the family could borrow about $137,000. If the required down-payment is 10%, the top sale price would be $152,222.
  - If the imposition of a $5,000 net development impact fee increases the sale price to $157,222, the down-payment rises by $500, the loan by $4,500 and the monthly mortgage payment by about $28.
  - Either the family finds an extra $500 for an upfront payment, and persuades the bank it can come up with the additional $28 per month, or the family looks for a cheaper lender or a different, house (costing $5,000 less).

Consequences of the Lack of, or of Low, Development Impact Fees: Effects for Households in Other Parts of the Jurisdiction

- **Cost to the Other Households:** The City of Lincoln has imposed modest development impact fees. Nevertheless, it is estimated that the costs of new development-required facilities, plus the upgrading of existing, will mean an extra $200 to $210 a year for "the average Lincoln household. . . by year four of the 12-year plan." About three-quarters of the extra taxes, it is estimated, will be allocated to cover the capital costs of new development.

Traits of Equitable Impact Fees: 2—Tailor Fees to the Best Estimates of the Actual Fiscal Impacts Created by the New Development

- The US Supreme Court requires a "reasonable relationship" between the fee and the estimated fiscal impacts (*Dolan v. City of Tigard* [Oregon], 1994). Exact correspondence between (a) the fees levied per new home or 1,000 square feet of commercial space and (b) the capital costs of providing those properties with services is *not* expected."
- As discussed earlier, Phoenix varies its fees by geographic area both for fairer calibration of fees and in order that the collected monies are spent only on facilities serving the development.
- Most of Lincoln's fees are standard across all geographic divisions but also may be spent, for most services, only in the same areas from which they were collected. Those areas are named "Water Distribution Benefit Districts 1 through 7," "Arterial Street Impact Fee Benefit District Nos. 1 through 7," and "Neighborhood Park and Trail Impact Fee Benefit District Nos. 1 through 7," as well as the "Water System Impact Fee District" and the "Wastewater Impact Fee Benefit District," both of which encompass the entire city.

2—Tailor Fees (continued)

- **Example:** The Village of Bartlett, Illinois (a western suburb of Chicago) enacted an ordinance in 1999 that required a new 3-bedroom single-family home to pay a total of almost $2,900 in impact fees to the schools, the Village, the Fire Protection District, the Park District, and the Library. The comparable fee for a 4-bedroom home was nearly $4,000 Why this big a difference?
- The school and road fees probably did not cover the full cost of building the facilities needed to serve the new developments. Why not?

2—Tailor Fees (continued)

- **When jurisdictions' fees are some fraction of the full costs, what should be the considerations that guide the choice of that fraction?**

  Example:
  - Let's say a reputable study indicates that 3-bedroom detached single-family homes built in the early 1980s sent on average one-third a student per dwelling unit to the local elementary schools over the following 20 years.
  - Let's say also that 20 years is the normal life of bonds for financing our schools.
  - Let's assume homes currently built will also require an average of one third of a seat over the next 20 years and that a single space in a new primary schools averages $10,000 in construction costs.
  - Should we charge new homes of the same size (3 bedroom detached) a gross impact fee of $3,333, then reduce it by the likely contribution to retiring the bonds that such homes will make through annual property taxes over the 20 years, and finally consider the balance as the community's contribution?

2—Tailor Fees (continued)
A Bad Example of Varying Fees?
What might be wrong with this schedule of fees?

Roundlake, Illinois Type of Dwelling Unit	School Impact Fee
Condos or townhouses with two bedrooms (BRs)	$1,000
Condos or townhouses with 3 BRs	$1,500
Rental apartments with 2 BRs	$3,500
Rental apartments with 3 BRs	$4,000
Single-family homes with 3 BRs	$3,500
Single-family homes with 4 BRs	$4,000

Traits of Equitable Impact Fees:
3-Provide for Regular Updating of Fees, Reducing Fees, Reimbursements, and Credits

- The *Lincoln ordinance* calls for reviewing the fee structure "at least once every three fiscal years to ensure" among other things that the fees charged do not "exceed the actual cost of constructing" the facilities required by the development.
- The *Phoenix ordinance* provides for reducing fees by estimates of the:
  - alternative revenues attributable to the development (such as "property taxes used to support capital expenditures and repayment, and water and sewer user fees that contribute to funding infrastructure projects") and
  - any other sources (e.g., state highway taxes).

  For example, in one Impact Fee district, the "Gross Impact Fee" of $7,713 per standard single-family home was offset by $2,854 in alternative revenues, leaving a "Net Impact Fee" of $4,859 collectible at the time building permits are purchased.
- The *Lincoln ordinance*:
  - refunds fees that have sat in the fee account for a particular kind of facility (e.g., arterial roads) for 8 years without being spent, or if the building permit for which the fee was paid expires "without possibility of further extension"; and
  - reimburses fees when the developer has contributed to finance an "Impact Fee Facility" or donated land for such a facility.

Traits of Equitable Impact Fees: 3—Flexibility in Application (continued)

- Both cities' ordinances provide for credits or offsets resulting from past and future contributions that the developments made or make to financing the capital facilities.
- Lincoln allows for landowners to apply for exemptions if they can demonstrate no additional demand for "a specific Impact Fee facility" beyond what was required before the development takes place.

Very expensive homes like these might possibly generate enough annual property tax revenues to cover the city's capital investments for servicing them (but probably not the school district's costs unless they are second homes or vacation homes).

Traits of Equitable Impact Fees: 4--Sequester Impact Fee Receipts so that They May be Spent only on Facilities Benefiting the Developments that Paid the Fees

- Lincoln's ordinance provides that "Impact fees shall be spent only within the benefit district in which they were collected" except for:
  - large wastewater and water system facilities that benefit both the districts from which the money came and the remainder of the city; and
  - arterial roads which border the Impact Fee Benefit District that generated the money.

  The fees are placed in "a separate impact fee account for each impact benefit district." That is, they should not be susceptible to being "raided" for other expenditure purposes.

Other Desirable Traits that May be Legislated into Development Impact Fee Ordinances

- Give the city council discretion to reduce fees? The Lincoln ordinance allows that: "In order to promote the economic development of the City or the public health, and general welfare of its residents, the City Council by an affirmative vote of at least five of its [seven] members may agree to pay some or all of the impact fees imposed on a proposed development or redevelopment from other funds of the City . . . ."
- Other desirable traits?

Questions for Discussion

- If the residents of sanitary sewer improvement districts pay for their services' capital improvements, should citizens of new developments in *incorporated* areas do the same, providing their property tax and other contributions to funding the same kinds of facilities are taken into account?
- Should community "A" not impose impact fees because community "B" and perhaps other rival communities are fee-less? What does community "A" lose if fee-less developments go to its rivals? What might it gain?
- If state law does not explicitly permit impact fees (such as for schools), are citizens interested in such fees out of luck?
- Sources for learning more about "development impact fees"? Do a "Google" Internet search for this topic. Look especially for work by Robert Burchell of Rutgers University, Arthur Nelson of Virginia Tech, Duncan Associates of Austin (TX), and Heartland Institute of Chicago.