BANKING ON TDRS: THE GOVERNMENT'S ROLE AS BANKER OF TRANSFERABLE DEVELOPMENT RIGHTS

SARAH J. STEVENSON*

INTRODUCTION

In 1972, Bernadine Suitum and her husband purchased land near the Nevada shore of Lake Tahoe to build a retirement home.[1] When they applied for a building permit in 1989, however, they were informed that their land had been declared a "Stream Environment Zone" (SEZ) in which development was prohibited for fear of causing soil erosion into the lake.[2] To reduce the Suitums' financial hardship, the Tahoe Regional Planning Agency granted them one transferable development right (TDR) and the chance to win more in a lottery.[3] These TDRs could only be sold to owners outside of the SEZ.[4] Mrs. Suitum is now an eighty-two-year-old widow, in fragile health, who does not know where to find a buyer for her TDR.[5] She owns property she cannot develop and a development right she cannot sell.

As Mrs. Suitum learned, development rights are property rights that can be severed from land and sold.[6] In this way, landowners realize some economic benefit from the sale of development rights they are no longer able to exercise due to government regulation. The right to develop property, much like the right to exclude trespassers, is one of many rights traditionally associated with ownership.[7] Develop-

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1 See Suitum v. Tahoe Reg'l Planning Agency, 117 S. Ct. 1659, 1663 (1997).

2 See id. at 1662-63.

3 See id. at 1663.

4 See id.

5 See Richard J. Lazarus, Litigating Suitum v. Tahoe Regional Planning Agency in the United States Supreme Court, 12 J. Land Use & Envtl. L. 179, 185 (1997).

6 See John J. Costonis, Development Rights Transfer: An Exploratory Essay, 83 Yale L.J. 75, 85 (1973) [hereinafter Costonis, Development Rights Transfer] (stating that "[d]evelopment rights transfer breaks the linkage between particular land and its development potential by permitting the transfer of that potential, or 'development rights'").

7 See, e.g., Jesse Dukeminier & James E. Krier, Property 86 (3d ed. 1993) ("The abstraction we call property is multi- not monolithic. It consists of a number of disparate rights, a 'bundle' of them: the right to possess, the right to use, the right to exclude, the right to transfer.").

ment can, however, be restricted or prohibited entirely, as in the case above. When development or use is so restricted that all economic value has been removed from the property, the government may face a challenge that it has effectively "taken" the property without providing just compensation.[8] TDRs are a land use tool that enables government to restrict development without actually taking, and paying for, property.

TDRs are the subject of an extensive body of written work.[9] In practice, TDRs have been widely accepted by land use planners and

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[8] The Fifth Amendment expressly prohibits taking private property for public use without providing just compensation. See U.S. Const. amend. V. Thus, under the Fifth Amendment, a takings claim requires two levels of analysis: an examination of public use or public purpose, and an analysis of just compensation. See infra Part III.A.4 (discussing the public use requirement). Just compensation has been found to be payment of fair market value, see, e.g., Coniston Corp. v. Village of Hoffman Estates, 844 F.2d 461, 464 (7th Cir. 1988). Where government regulation of property "goes too far," Pennsylvania Coal Co. v. Mahon, 260 U.S. 393, 415 (1922), or interferes with "distinct investment-backed expectations" such that an owner is deprived of a "'reasonable return,'" Penn Cent. Transp. Co. v. New York City, 438 U.S. 104, 127, 136 (1978), it may be recognized as a taking, prompting public purpose and just compensation analyses.

[9] See, e.g., David Berry & Gene Steiker, An Economic Analysis of Transfer of Development Rights, 17 Nat. Resources J. 55, 55 (1977) (analyzing economics of TDRs); John J. Costonis, The Chicago Plan: Incentive Zoning and the Preservation of Urban Landmarks, 85 Harv. L. Rev. 574, 574 (1972) [hereinafter Costonis, The Chicago Plan] (outlining TDR scheme designed to preserve urban historic landmarks and responding to various challenges such scheme presents); Costonis, Development Rights Transfer, supra note 6, at 85 (exploring benefits of applying TDR scheme, modeled on Chicago Plan, to protect various resources); Jerold S. Kayden, Market-Based Regulatory Approaches: A Comparative Discussion of Environmental and Land Use Techniques in the United States, 19 B.C. Envtl. Aff. L. Rev. 565, 565-66 (1992) (examining market based regulatory approaches in land use regulation, focusing on incentive zoning and transfer of development rights); Norman Marcus, Air Rights in New York City: TDR, Zoning Lot Merger and the Well-Considered Plan, 50 Brook. L. Rev. 867, 867-68 (1984) [hereinafter Marcus, Air Rights in New York City] (tracing history of New York's use of TDRs, examining legal and practical limitations, and evaluating City's successes and failures); Norman Marcus, Transferable Development Rights: A Current Appraisal, Prob. & Prop., Mar.-Apr. 1987, at 40 [hereinafter Marcus, Transferable Development Rights] (critiquing expanded use of TDRs and describing legal hurdles posed by their use); Dennis J. McEleney, Using Transferable Development Rights to Preserve Vanishing Landscapes and Landmarks, 83 Ill. B.J. 634, 634 (1995) (exploring use of TDRs as preservation method); James M. Pedowitz, Air Space, Air Rights and Transferable Development Rights, in Title Insurance 1990: The Basics and Beyond, at 231 (PLI Real Estate Law and Practice Course Handbook Series No. N4-4540, 1990) (exploring distinctions between use of air space, air rights, and TDRs in land use planning); David Alan Richards, Downtown Growth Control Through Development Rights Transfer, 21 Real Prop. Prob. & Tr. J. 435, 435 (1986) (evaluating New York's experience with TDRs); James T.B. Tripp & Daniel J. Dudek, Institutional Guidelines for Designing Successful Transferable Rights Programs, 6 Yale J. on Reg. 369, 370 (1989) (examining use of TDRs to solve environmental problems by looking at two successful programs and extrapolating essential guidelines for use in other environmental contexts).

courts alike, and are integral pieces of many land use schemes.[10] In spite of their broad application, TDRs may face a number of obstacles, the most significant of which is difficulty in valuation.[11] Unlike real estate, TDRs do not have a traditional fair market and often no known or guaranteed value. This creates problems not only for landowners, as seen above, but also for governments trying to avoid a taking. Many landowners are unfamiliar with TDRs and are reluctant to purchase them. This reluctance is exacerbated by restrictions on transferability; TDRs may only be purchased and used by landowners in designated receiving areas.[12] These restrictions also lead to timing difficulties; without a middleman to buy and hold the TDRs, mutually beneficial transactions can take place only if a seller and a buyer are simultaneously ready to sell and develop.[13] In spite of these problems, TDRs continue to be a desirable land use tool because they provide governments flexibility in planning without the high cost of outright property acquisition.[14]

TDR banks were created to counter some of the difficulties posed by the use of TDRs. Government operated TDR banks resolve valuation and marketability problems by setting minimum purchase prices, guaranteeing loans that use TDRs as collateral, and purchasing the

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10 See Madelyn Glickfeld, Update on Transfer of Development Rights, at 1375, 1378 (ALI-ABA Course of Study Materials: Planning, Regulation, Litigation, Eminent Domain, and Compensation No. C431, 1989) (asserting that national survey which identified over 30 active TDR programs actually undercounted). TDRs are being used in a variety of preservation efforts, including the preservation of historic landmarks, valuable ecosystems, agricultural land, open space, and low-income housing. See infra Part II.

11 Valuation goes to the takings issue, see supra note 8. If a government is using TDRs to offset economic loss as a result of land use regulation, the TDRs must have some value. See Berry & Steiker, supra note 9, at 62.

12 See, e.g., Costonis, Development Rights Transfer, supra note 6, at 86 (observing that only designated owners are able to receive TDRs under Chicago Plan).

13 See, e.g., Lois Weiss, Air Rights Market Heats Up; Transferable Development Rights, Real Estate Weekly, Jan. 14, 1998, at 1 (quoting Manhattan brokerage partner as saying TDRs are valuable if there is potential receiver, but without one, "they have little to no value"). The elaborated benefits of a TDR bank also illustrate the potential severity of this restriction. See, e.g., Joseph D. Stinson, Note and Comment: Transferring Development Rights: Purpose, Problems, and Prospects in New York, 17 Pace L. Rev. 319, 329-30 (1996) (stating development rights bank can facilitate transactions by giving property owners option of selling to bank when development demand is low); Roger K. Lewis, Little-Used Zoning Strategy Could Keep Suburban Sprawl in Check, Wash. Post, Nov. 16, 1996, at E1 (stating that TDR bank permits jurisdiction to ensure preservation of precious land by acquiring and banking development rights without waiting for developers).

14 See Berry & Steiker, supra note 9, at 58:

> When compared along three major criteria, cost to the public, effectiveness in preserving . . . , and the issue of taking private property without compensation, transferable development rights (TDRs) fare very well on paper. . . . Each of the other [prominent] methods [of public preservation] fares worse on at least one of the three criteria.

TDRs outright.[15] By acting as a middleman between buyer and seller, TDR banks fill a critical timing gap that could be the downfall of a TDR program. A TDR bank may also act as a clearinghouse and an information source, helping to match buyers with sellers and assisting with transactions.[16] Additionally, a TDR bank may serve as the administering body for a complex TDR program and may even generate funds so that the TDR program becomes self-sustaining.[17]

This Note examines government operated TDR banks and their capacity to overcome obstacles hindering otherwise successful TDR programs. Many commentators have addressed TDR banks in the context of TDR programs in general;[18] this Note provides the first comprehensive analysis of TDR banks, examining the legitimacy of the banks themselves and, ultimately, their role in successful TDR programs. As the number of localities turning to TDR programs and banks increases,[19] it is likely that challenges to their use will also increase. It is hoped that this Note will prove useful to localities as they establish their own TDR banks, and that the analysis contained in Part III will help them avoid legal and financial difficulties that may interfere with the effective preservation of valuable public goods.

Part I outlines the evolution of TDRs and the creation of TDR banks, including an examination of New York City's landmarks preservation program and Professor John J. Costonis's "Chicago Plan," the first comprehensive TDR scheme designed to integrate a government operated TDR bank. Part II then depicts four TDR schemes to help illustrate the different ways in which TDRs can be used, as well

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15 See, e.g., infra Part II.B (discussing role of New Jersey's Pinelands Development Credit Bank).

16 See Tripp & Dudek, supra note 9, at 377 (stating that "[p]rograms can be especially effective by providing for 'credit banks'" to "help buyers and sellers of rights identify one another, and to help broker transactions").

17 See infra Part II.C (discussing role of TDR bank in Seattle, Washington's TDR program).

18 See supra note 9 and sources cited therein.

19 See Roger K. Lewis, Little-Used Zoning Strategy Could Keep Suburban Sprawl in Check, Wash. Post, Nov. 16, 1996, at E1 ("TDR is still in its infancy. But in the next century, it is sure to become one of the most powerful growth management tools, more the norm than the exception."). Compare Eugene L. Meyer, Saving Farmland: Citizens Oppose County Plan to Preserve Its Open Spaces, Wash. Post, July 7, 1982, at C1 ("When first proposed for Montgomery in 1980, the TDR concept was so obscure that nobody came to the first hearing."); and Kathryn Tolbert, How to Sell the Farm and Keep It, Too; Montgomery's Farm Preservation Plan; Real Estate Roulette, Wash. Post, Mar. 12, 1981, at Md.1 ("There are few other places in the nation where such a system has been tried . . . .") with Lois Weiss, Air Rights Market Heats Up; Transferable Development Rights, Real Estate Weekly, Jan. 14, 1998, at 1 ("But as development once again becomes commonplace and assemblages to create large parcels harder to accomplish, the transferable development rights (TDR), or air rights, are enjoying a burst of value.").

as to highlight the function of TDR banks in these various programs. Part III analyzes legal and financial issues that TDR banks may encounter. This Note concludes that TDR banks provide significant benefits to TDR programs, with minimal risk that any potential challenges will preclude their use or negatively affect a TDR program. Careful design of a TDR bank, as well as diligent monitoring of program administration, will help avoid potential problems and ensure that the costs imposed by TDR banks are far outweighed by the benefits they confer.

I
The Advent of Transferable Development Rights and TDR Banks

A. *The Evolution of TDRs*

An examination of TDR banks requires a brief look at the evolution of TDRs as a land use tool. In the late nineteenth and early twentieth centuries, the advent of skyscrapers and increased downtown development led many American cities to impose growth restrictions.[20] New York City passed its first zoning resolution in 1916,[21] imposing height[22] and area limitations[23] on building size and ultimately regulating maximum building bulk.

The first comprehensive amendment of New York's 1916 Zoning Resolution took effect in 1961.[24] This legislation amended the zoning resolution, as it relates to TDRs, in three significant ways. First, it created the floor area ratio, or FAR, to regulate development.[25] Sec-

20 See Richards, supra note 9, at 435-42 (describing imposition of development restrictions in Boston, New York, and Chicago).

21 See New York, N.Y., Zoning Res. (1916); New York City Planning Comm'n, Report N 820253 ZRM, 9 (1982).

22 See New York, N.Y., Zoning Res. §§ 8-9 (1916).

23 See id. §§ 10-18.

24 See New York, N.Y., Zoning Res. (1961).

25 See id. § 33-11; New York City Planning Comm'n, Report N 820253 ZRM, 9 (1982). Floor area ratio (FAR) is the multiple used to determine the maximum allowable floor area for a development. If, for example, a 75,000 square foot lot was zoned FAR 15, it would have a maximum floor area of 1,125,000 square feet (75,000 x 15). See Marcus, Air Rights in New York City, supra note 9, at 870 n.13. In New York, both FAR and tower coverage are strictly zoned. Tower coverage refers to the percentage of the building's zoning lot that is covered by its tower, or skyscraper. See id. at 889 n.66. Prior to 1961, the FAR was not actually controlled. Rather, if a tower (skyscraper) occupied less than 25% of the lot area, it was allowed to exceed height and setback limitations. See New York, N.Y., Zoning Res. § 9(d) (1916). Developers were allowed to combine contiguous parcels, thereby increasing their height restrictions, which resulted in a number of famous Manhattan skyscrapers, such as the Empire State Building and 666 Fifth Avenue. See Marcus, Air Rights in New York City, supra note 9, at 872-73. Because tower coverage was determined by lot area, the size of the lot was significant. Under the 1916 resolution a "lot" was de-

ond, in order to appease developers who had been lobbying for increased bulk regulations, the 1961 amendment incorporated a bonus program which granted an increase in the FAR if a plaza surrounded the building.[26] Third, the legislation redefined the zoning lot, allowing FAR to be calculated including any other parcel in the same city block owned or controlled through a lease of at least 75 years.[27] In effect, owners in the same city block were allowed to transfer development rights from one parcel to another.[28]

In 1965, New York adopted a Landmarks Preservation Law which enabled the City to designate historic landmarks and regulate any alterations to their use or physical structure.[29] Landmark owners were sometimes granted TDRs to compensate for the development restrictions that accompanied historic designation. In 1968, to make the 1961 transferable development scheme more effective for the preservation of such landmarks, the New York Zoning Resolution was amended again.[30] This amendment expanded the available receiving lots by redefining "adjacent" transferee lots to include those across a street or intersection from the landmark.[31] This gave landmark owners additional opportunities to sell their TDRs. The amendment benefited landmark owners by increasing opportunities for the realization of economic gain and simultaneously benefited the City by increasing tax revenues.[32] This amendment was the first example of "beyond-

fined to include contiguous parcels held in common ownership or in separate ownership, as long as one of the parcels benefited from the adjoining parcel's air rights by way of an air rights sale, lease, or other conveyance. See id. at 871-72 .

26 See New York, N.Y., Zoning Res. § 33-13 (1961); New York City Planning Comm'n, Report N 820253 ZRM, 9 (1982).

27 See New York, N.Y., Zoning Res. § 12-10 (1961); see also Marcus, Air Rights in New York City, supra note 9, at 873-74; Richards, supra note 9, at 442-45. The 1961 definition, which allowed a long term lease to qualify as ownership for purposes of transferring development rights, was somewhat problematic. Termination of leases for failure to pay the rent or mortgage created problems. If the transferred development rights had already been used, the unimproved parcel was left permanently deprived of its rights; in the alternative, the City faced overbuilding if it allowed the unimproved parcel to build to its originally allowable FAR. See Marcus, Air Rights in New York City, supra note 9, at 874-75. Because of these problems, § 12-10 has been amended to require a permanent transfer of development rights from one owner to another. See New York, N.Y., Zoning Res. § 12-10 (1998); New York City Planning Comm'n, Report N 760226 ZRY (1977) (describing problems with leasehold provision and proposing amendment to § 12-10).

28 See Marcus, Air Rights in New York City, supra note 9, at 873-74.

29 See New York, N.Y., Admin. Code, ch. 8-A, § 205-1.0 (1976).

30 See New York, N.Y., Zoning Res. § 74-79 (1998).

31 See id.

32 See New York City Planning Comm'n, Report CP-20253, 303 (1968) (listing benefits of amendment, including, "most importantly, [that the City] can benefit by new tax revenues from what was previously untaxable"). Prior to this amendment landmark owners were compensated with tax relief rather than TDRs. See Richards, supra note 9, at 448-49.

the-block" TDR use, drastically changing the concept of, and traditional justifications for, TDRs.[33]

Thus, there developed two distinct kinds of TDRs in New York City—the traditional transfer, or zoning lot merger, that allowed transfers between owners (or lessors) of contiguous lots, and the new, more controversial TDR that allowed transfer from one owner to another, from one lot to a completely separate parcel. New York continues to permit the former type of zoning lot mergers, which are distinct from the TDRs discussed in this Note, on an as-of-right basis.[34] The latter type of TDR is a more flexible zoning device and presents the potential for much more creative use. Many local governments are recognizing the benefits of these TDRs and are implementing land use schemes utilizing them as their centerpiece to preserve public goods such as historic buildings, endangered ecosystems, and low-income housing.[35]

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[33] Previously, transfers had been allowed only to contiguous or same-block zoning lots. This seemingly small step across the street was actually the first of many leaps that resulted in TDR schemes with sending and receiving parcels separated by miles. Some commentators sharply criticize this extension of the TDR as destructive of zoning plans. For example, Norman Marcus, former General Counsel of the New York City Planning Commission, wrote:

> Many planners feel that the essential interrelationship of zoning density controls . . . and other objects of planning concern could not survive if the city allowed indiscriminate transferability of unused development rights between more widely spaced parcels. At its extreme, if development rights were transferable from Staten Island to the Bronx, for example, TDR would destroy any zoning plan within which it operates.

Marcus, Air Rights in New York City, supra note 9, at 878 n.40.

In addition to the practical problems presented by long distance transfers, these schemes upset the traditional reciprocity of benefits justification of TDRs. For example, height restrictions on a historic landmark create open space which traditionally has been thought to counterbalance the additional height of a neighboring transferee building. The shadow cast by the extra height is offset by the light resulting from the less developed landmark. Neighboring parties who bear the burden of additional density, therefore, also reap the benefit of open space created by height restrictions. Where TDRs are not transferred to contiguous lots, there is a risk that certain areas will suffer the burdens of overdensification, and an accompanying overuse of public services, without enjoying the aesthetic benefit created by the landmarked sending lots. See id. at 896.

[34] See New York, N.Y., Zoning Res. § 12-10 (1998) (allowing owner(s) of contiguous lots to merge lots, as-of-right, in order to transfer development rights of one to other). For more on as-of-right zoning lot mergers, see David Alan Richards & David M. Goldberg, Development Rights Transfer Documentation: From Proposal to Partnership, in Air Rights, Air Space, and Transferable Development Rights, at 139 (PLI Real Estate Law and Practice Course Handbook Series No. 269, 1985); see also Marcus, Air Rights in New York City, supra note 9, at 870-71.

[35] See, e.g., Glickfeld, supra note 10, at 1378-79 (listing Denver, Colorado; San Francisco, Marin County, Santa Monica, and Oxnard, California; Monroe County and Hollywood Beach, Florida as localities that have used TDRs); Kayden, supra note 9, at 577 (naming Burlington County and Chesterfield Township, New Jersey as localities with TDR programs); Ellen M. Randle, Article and Comment: The National Reserve System and

The new form of TDR was validated in dicta by the Supreme Court in *Penn Central Transportation Co. v. New York City*.[36] In that case, Penn Central asserted that New York City's decision to landmark Grand Central Station, thereby restricting its development rights, effected a taking.[37] The Court did not find a taking.[38] The Court further stated that while the City's grant of TDRs "may well not have constituted 'just compensation' if a 'taking' had occurred, the rights nevertheless undoubtedly mitigate whatever financial burdens the law has imposed . . . ."[39] The Supreme Court's implicit acceptance of the use of TDRs in *Penn Central* was an extremely important evolutionary step for TDRs. It signaled to New York City, and the rest of the country, not only that this new form of TDR was an acceptable land use tool, but also that TDRs had some recognizable value that could mitigate financial hardship.[40] The Supreme Court left open the question of how to determine the value of TDRs, however, leaving room for confusion.[41]

Transferable Development Rights: Is the New Jersey Pinelands Plan an Unconstitutional "Taking"?, 10 B.C. Envtl. Aff. L. Rev. 183, 205 n.211 (1982) (listing Chesterfield and Hillsborough, New Jersey; Eden and Southhampton, New York; Windsor, Connecticut; Birmingham, Buckingham, and Upper Makefield, Pennsylvania; Calvert County, Maryland; Collier County and St. Petersburg, Florida; and Santa Monica-Malibu, California as localities with TDR programs); see also Part II, infra.

36 438 U.S. 104 (1978).

37 See id. at 119.

38 See id. at 138. The Court did not find a taking because it determined that the landmarking reasonably promoted the general welfare and did not destroy the economic value of the property. See id. Penn Central, as owner of Grand Central, was able to earn a "reasonable return" without further developing the terminal. Id. at 136. The Court also concluded that Penn Central "exaggerate[d] the effect of the law on [its] ability to make use of the air rights" in two ways. Id. First, the law did not prohibit use of all air rights above the station—this case simply determined that the particular 50-story office building proposed was unacceptable. See id. Second, the Court found that the granting of TDRs by the City meant that Penn Central's "ability to use [the air] rights ha[d] not been abrogated." Id. at 137. Thus, the Court mentioned TDRs in dicta but did not find a taking and so never reached the question of whether TDRs constitute just compensation within the meaning of the Fifth Amendment.

39 Id. at 137.

40 See, e.g., Marcus, Air Rights in New York City, supra note 9, at 890 ("The *Penn Central* decision was vitally important for the continuation of TDR in New York City. In validating the Landmarks Preservation Law and its supportive TDR options . . . the Supreme Court allowed the city to consider and develop new occasions for using TDR to further its other planning goals.").

41 In his dissent, Justice Rehnquist more directly addressed the valuation problems of TDRs than did the majority, focusing on the difficulty of determining TDRs' value given restrictions on transferability and their uncertain marketability. See *Penn Central*, 438 U.S. at 151-52 (Rehnquist, J., dissenting).

B. *Identifying and Resolving the Trouble with TDRs*

Since *Penn Central*, TDRs have been adapted to facilitate a variety of land use schemes.[42] Although widely used, some TDR programs continue to be afflicted by the same difficulties that posed problems for New York and Penn Central in 1978. Valuation and marketability remain the two most significant obstacles facing TDR programs. Because the Supreme Court did not reach the issue of valuation in *Penn Central*, and most areas still do not have a fair market for development rights,[43] the question of how to determine the value of TDRs remains open. Additionally, restrictions on transfer create timing issues for buyers and sellers. Sellers, who may only sell TDRs to buyers in designated receiving districts, may find themselves unable to realize the value of a TDR if buyers are not ready to develop.

These problems are not insurmountable. As early as 1971, Professor John J. Costonis of the University of Illinois College of Law proposed a TDR program that solved the problems of speculative valuation and timing by creating a "TDR bank" and giving landowners the option of selling their TDRs to the bank for cash.[44] This would guarantee a value and a buyer for the development rights.

Costonis designed his plan to help preserve Chicago's urban landmarks.[45] He recognized that New York City's use of TDRs in its landmarks preservation program constituted a "giant step" in the right direction, but he did not feel that the program had been extremely successful.[46] Costonis identified five major drawbacks to New York's TDR program.[47] The first of these drawbacks was the absence of a "rational incentive structure" for inducing landowners to preserve their landmarks willingly.[48] Limiting development rights transfers to adjacent lots or across the street drastically restricted the potential buyers of the rights.[49] The small pool of potential buyers meant that landmark owners might have a hard time finding a purchaser and, in

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[42] See supra notes 10, 35.

[43] Fair market value is commonly used as a measure of value for taken property. See supra note 8.

[44] See Costonis, Development Rights Transfer, supra note 6, at 87 (describing aspect of Chicago Plan in which landmark owner would be entitled to sell unused development rights to owners in designated transfer district, or receive cash award from TDR bank in exchange for preservation restriction).

[45] See Costonis, The Chicago Plan, supra note 9, at 574-75 (explaining importance of preserving historic buildings).

[46] See id. at 584; see also id. at 578 (observing that although New York's transfer program was adopted in 1968, no transfer had taken place by 1972).

[47] See id. at 586.

[48] See id. at 586-87.

[49] See id. (stating that "the plan is useful only when a developer can be found who happens to own a lot located across a street or an intersection from a landmark").

the absence of competition for the TDRs, would probably receive a low price. Additionally, any transfer was necessarily conditioned on construction activity in the immediate vicinity of the landmark.[50] These concerns were ultimately expressions of valuation and timing problems, which presented legal difficulties like those addressed in *Penn Central*,[51] as well as practical complications. If a landmark owner could not get enough in exchange for his TDRs, he might not be able to maintain the landmark adequately.

The second weakness Costonis identified was the "labyrinthine procedures governing the issuance of transfer permits."[52] The discretionary decisions that followed designation as a New York landmark, especially the approval of a transferee lot, did not attract voluntary participation in the program.[53] Costonis believed that many landowners opposed designation, resulting in the loss of valuable landmarks, because of "reasonable fears" that the discretion granted to local commissions would lead to negative economic effects.[54] Third, Costonis feared that the New York plan relied too heavily upon the voluntary participation of landmark owners, who might balk at the legality and marketability of TDRs.[55] Fourth, Costonis questioned New York's ability to guarantee that the landmarks would actually be preserved.[56] He saw no mechanism for defining the obligations assumed by the present and future owners of the landmark as a consequence of development rights transfer. Additionally, it appeared that if the owner chose to demolish the landmark it "'could be replaced . . . by another building with the same amount of floor space.'"[57] The TDRs simply served to "reduce[ ] much of the economic pressure" to convert the landmark to a more profitable use.[58] Costonis wanted a much stronger guarantee that the landmark would actually be preserved. Finally, Costonis predicted that the adjacency requirement[59] would re-

[50] See id. at 587 (noting that extra floor space, or development rights, may be worthless if no construction is contemplated on eligible sites adjacent to landmark).

[51] See supra note 41 (noting dissent's treatment of valuation problems).

[52] Costonis, The Chicago Plan, supra note 9, at 587.

[53] See id. (explaining that "battle to safeguard threatened buildings of landmark quality [was] often lost" because owners fought so hard to avoid designation).

[54] See id. (explaining that transfer permits are issued after designation, so owners do not know what they will get in lieu of development rights until it is too late to negotiate).

[55] See id. at 588.

[56] See id.

[57] Id. at 588 n.50 (quoting Frank Gilbert, Saving Landmarks, Hist. Preservation, July-Sept. 1970, at 14).

[58] Id.

[59] Even with the expanded definition of adjacent lots allowed under the 1968 amendment, transfers could be made no farther than across a street or intersection. See supra note 49.

sult in poor urban design.[60] He feared that mammoth concentrations of bulk in one block might overtax services, increase traffic, or destroy the visual enjoyment of a landmark by blocking it from sight.[61] Costonis proposed a plan that would improve upon New York's program, designed specifically for implementation in Chicago; hence, the "Chicago Plan."[62]

Costonis's Chicago Plan[63] called for the designation of a "development rights transfer district," within which unused development rights could be transferred.[64] This district would be drawn to include the downtown area where most of the landmark sites were located.[65]

Upon designation as a landmark, a building's owner would be entitled to sell unused development rights to owners of nonlandmark sites in the transfer district.[66] There would be limits on the number of TDRs any one parcel could purchase in order to prevent overbuilding, but a landmark owner could transfer development rights to many different sites if necessary.[67] The sale of TDRs would create a "dual bulk" system of zoning, in which purchasers of TDRs would be allowed to build beyond the maximum development limits in the transfer district.[68]

Costonis's plan also called for the creation of a TDR bank. This bank would have the power to buy and sell development rights.[69] Costonis envisioned the TDR bank raising funds, at least initially, through the sale of publicly owned landmark TDRs.[70] The bank would then continue to finance program costs through the sale of de-

60 See Costonis, The Chicago Plan, supra note 9, at 589.

61 See id.

62 The Chicago Plan was never implemented in Chicago. It has, however, served as a model for many other municipalities' TDR programs.

63 The following description of the Chicago Plan is taken from Costonis, Development Rights Transfer, supra note 6, at 86-87.

64 See id. at 86.

65 This inclusion served three purposes: a downtown area would probably offer the most lucrative market for TDRs because land values were likely to be high; low density landmarks would offset the increased density permitted on transferee sites; and the area would probably contain a high concentration of city public services, enabling it to handle the redistributed density resulting from the transfer. See id.

66 In addition to receiving the sale price of the TDRs, landmark owners would enjoy a reduction in real estate taxes, as the appraised value of the landmarked property would be reduced by the amount of the transferred value. In exchange, owners would be obligated by a preservation restriction to maintain the landmark in accordance with certain standards. See id. at 86-87.

67 No transferee lot could increase its constructive lot area by more than 15%, a figure on which municipal planners and architects in Chicago concurred. See Costonis, The Chicago Plan, supra note 9, at 590 & n.55.

68 See Costonis, Development Rights Transfer, supra note 6, at 87.

69 See id.

70 See id.

velopment rights it had purchased from landmark owners. The bank would be subject to the same controls imposed on private sellers and purchasers. To ensure that the goal of preservation was actually achieved, the TDR bank would make additional subsidies available to landmark owners to cover maintenance and restoration costs that exceeded the amount received from the sale of TDRs.[71] Additionally, the bank would fund acquisition costs of easements or preservation restrictions from owners who did not voluntarily participate in the TDR program. If a landmark owner rejected the transfer option or wanted immediate compensation for his development rights, the City, funded by the bank, would purchase or condemn unused development rights.[72]

The TDR bank would serve as a pool for rights acquired from unwilling landmark owners, as described above, as well as those rights donated by other owners or transferred from publicly owned landmarks.[73] Federal, state, and local tax deductions, as well as reduced property taxes, would serve as incentives for individuals to donate their development rights.[74]

Costonis's plan addressed many of the problems experienced in New York. It provided funds to enable landmark owners to maintain historic buildings, which can be costly, and ensured preservation of valuable public goods without shifting the negative externalities of such preservation onto owners.[75] The plan guaranteed a buyer for TDRs—if the landmark owner could not find a third party buyer, the TDR bank would purchase the TDRs.[76] Costonis also provided a way for the City to finance such a program without expending tax dollars or losing much tax revenue.[77] Tax abatements, previously used as in-

[71] See Costonis, The Chicago Plan, supra note 9, at 592.

[72] See Costonis, Development Rights Transfer, supra note 6, at 87.

[73] See id.

[74] See Costonis, The Chicago Plan, supra note 9, at 598.

[75] Valuable downtown real estate is often worth much more if sold and converted from high maintenance historic landmarks to new development. Owners who choose, or who are forced, to preserve often lose large amounts of money by not selling their property. See Berry & Steiker, supra note 9, at 56 ("[T]he economic penalty for not participating in speculation and conversion falls heavily on the preservationist so that maintaining current uses during this rush to speculate and convert is often difficult.").

[76] See Costonis, Development Rights Transfer, supra note 6, at 86-87.

[77] Historically, one of the problems afflicting landmark preservation programs is that landmark ownership in areas of high land value is significantly less profitable than redevelopment. This leads private owners to fight landmark designation. Forced designation is not only politically unpopular, but also risks being found unconstitutional due to the economic hardships imposed on landowners. Cities themselves are often unable to budget large sums for acquisition and maintenance of landmarks due to various higher priority demands on the municipal fisc. TDRs appear to present an optimal solution, at very low cost to municipalities. See Costonis, The Chicago Plan, supra note 9, at 579-84 & 583 n.36.

centives for owners to maintain landmarks, would no longer be necessary. Instead, the offer of TDRs and subsequent tax reductions, due to a drop in appraised real estate value which takes place when a building is designated as a landmark, would attract landmark owners.[78] The tax reductions would then be offset by increased taxes paid by purchasers of TDRs, due to an increase in value on the developed transferee sites.[79]

Even before the Supreme Court wrangled with the issue in *Penn Central*, the New York Court of Appeals had endorsed Costonis's approach. In *Fred F. French Investing Co. v. City of New York*,[80] the court held unconstitutional a zoning regulation that granted TDRs to compensate French for permanently zoning its land as two public parks.[81] Chief Judge Breitel wrote that the value of the TDRs was too uncertain to compensate adequately for the deprivation of "reasonable income productive or other private use" of the property.[82] Breitel cited to Costonis's plan and explicitly recommended using a "development bank" to purchase the TDRs, thereby guaranteeing a market value for the rights.[83]

C. *The Transferable Development Rights Bank*

A government operated TDR bank was an integral piece of Costonis's plan. Today TDR banks provide solutions to the greatest challenges facing TDR schemes by guaranteeing an owner something of value in exchange for unused development rights.[84] If the owner

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78 See id. at 592-93.

79 See id. at 591.

80 530 N.E.2d 381 (N.Y. 1976).

81 See id. at 383 (explaining that parks had previously been private but were rezoned as public parks after new owner announced plans to erect buildings in their place).

82 Id.

83 See id. at 388 (citing Costonis, Development Rights Transfer, supra note 6, at 86-87). The decision also contains an eloquent and entertaining commentary on the abstract nature of TDRs. Chief Judge Breitel described them as:

> [F]loating development rights, utterly unusable until they could be attached to some accommodating real property, available by happenstance of prior ownership, or by grant, purchase, or devise, and subject to the contingent approvals of administrative agencies. In such case, the development rights, disembodied abstractions of man's ingenuity, float in limbo until restored to reality by reattachment to tangible real property. Put another way, it is a tolerable abstraction to consider development rights apart from the solid land from which as a matter of zoning law they derive. But severed, the development rights are a double abstraction until they are actually attached to a receiving parcel . . . . [T]his leaves the granting parcel's owner's development rights in limbo until the day of salvation, if ever it comes.

Id. at 597-99.

84 See supra Part I.B (discussing potential resolutions to obstacles facing TDR programs).

cannot, or chooses not to, sell his TDRs himself, the bank will step in and purchase them. TDR banks are often mandated by statute to pay a particular minimum[85] or maximum[86] value for TDRs, and sometimes rely on real estate appraisals to determine the value of TDRs for individual properties.[87] Under any method, the goal is to guarantee landowners a fair price for their TDRs, so that restrictions on development do not create takings of property without just compensation.[88] A guaranteed purchaser and price serve to resolve speculative value issues, as well as to fill any timing gap that might result from the lack of an immediate buyer. In the end, landowners receive cash in exchange for development restrictions on their property, the government takes title to the development rights, and then recoups the purchase price by selling them later,[89] and most importantly, valuable public goods are preserved.

In addition to resolving issues of timing and speculative valuation, TDR banks help reduce transaction costs of buyers and sellers and improve administrative efficiency, thereby reducing governmental transaction costs.[90] These costs can be high and can affect all participants in the program.[91] Municipalities must determine how best to grant or distribute the TDRs, issue them to the appropriate parties, and maintain records of each TDR and how it is used.[92] Landowners

[85] See, e.g., N.J. Stat. Ann. § 13:18A-34 (West 1997) (setting minimum purchase price at $10,000 per Pinelands Development Credit).

[86] See, e.g., Seattle, Wash., Ordinance 116366 § 2 (Sept. 28, 1992) (designating maximum values to be paid for particular properties).

[87] See id. (leaving price per square foot to be determined by appraiser, within limits).

[88] See, e.g., Gardner v. New Jersey Pinelands Comm'n, 593 A.2d 251, 259-60 (N.J. 1991) (holding use restrictions imposed on farm did not result in taking). The Supreme Court of New Jersey also analogized New Jersey landowners' ability to receive and sell Pineland Development Credits (TDRs) to the Supreme Court's finding in *Penn Central* that the ability to transfer "valuable property rights" to other properties offset Penn Central's loss. See id. at 260-61; see also supra note 8 (discussing government regulations and takings law).

[89] Because of increasing real estate values in downtown and urban growth areas, this Note assumes that in most cases the value of development rights will increase, resulting in profit for whatever entity invests in TDRs for later resale.

[90] See Telephone Interview with John Ross, Executive Director, N.J. Pinelands Development Credit Bank (Mar. 31, 1998) (stating that "bank may be a misnomer"—it is really agency that "coordinates" and "monitors" program, and "helps bring parties together for sales").

[91] See Kayden, supra note 9, at 578-79 (noting that TDR programs tend to experience high transaction and administrative costs).

[92] James Tripp and Daniel Dudek surveyed a range of TDR programs and extrapolated eight basic design guidelines for a successful TDR program. These eight guidelines are: clear legal authority, technical capability to design and implement, exclusive control, clearly specified objectives, regional significance, economic value and incentives, equitable and administrative simplicity, and minimal transaction costs. See Tripp & Dudek, supra note 9, at 374-77. One essential component they list is an agency with the technical capac-

must find a purchaser for their TDRs, engage in time consuming negotiations over price, and prepare purchase agreements and other documents. Buyers must engage in timely market evaluations to determine how much TDRs are worth to their developments. The buyer must then seek a seller or, in many cases, multiple sellers in order to acquire sufficient numbers of TDRs, and then engage in negotiations and acquisitions. Approval of the transfer by the zoning body is often a prerequisite to final sale of the TDRs. These transactions must then be duly recorded with the locality which monitors development and TDR transfer ceilings.[93] The time and costs involved in these processes can be significant and can discourage optimal TDR exchanges.

A TDR bank helps to expedite the process, benefiting the community as a whole, as well as individual buyers and sellers of TDRs. Inasmuch as valuation difficulties compound transactional problems, a bank creates an initial market and ensures that a minimum price will be paid, thereby establishing parameters for valuation. To a certain extent valuation will be unique to each transaction,[94] but, as with any unique commodity, a general market price will help both the buyer and the seller ensure that they are engaging in a mutually beneficial exchange.[95] In addition, by pooling development rights a bank enables small holders to receive a competitive price for their TDRs and makes it easier for purchasers to buy large numbers of TDRs in a single transaction.

If a government operated TDR bank is also the entity facilitating TDR transactions, it offers another benefit—it can notify itself automatically of the transfer. The bank will be able to update TDR records instantly, avoiding the delay of verifying that the transaction

ity to design and implement a TDR program, "includ[ing] the capacity to establish baseline conditions, to certify the proper issuance and use of rights, and to monitor transactions in rights." Id. at 375. They also note that monitoring should be accompanied by a means to impose penalties for noncompliance with program regulations. See id. A singular agency responsible for both TDR transactions and monitoring may well give rise to economies of time and scale, thereby easing the operation and improving the efficiency of a TDR scheme.

93 Transfer ceilings are generally set at 15-20% over standard zoning allowed. See, e.g., supra note 67.

94 See Kayden, supra note 9, at 578 (describing valuation problems that plague TDR buyers and sellers alike).

95 Buyers and sellers conduct cost benefit analyses based on their best information about the value of the item being exchanged, as well as the relative worth of the item to them personally. Without prior sales, landowners and developers will have no idea how much a TDR might be worth. The price set by a TDR bank helps establish a baseline by which to measure the value of each individual transaction.

abides by program parameters.[96] All of these time saving functions will result in cost savings as well.

The benefits conferred by TDR banks help ease the implementation of TDR programs and greatly enhance their potential for success. This has become increasingly important in light of the widespread use of TDRs to achieve a broad range of planning and public policy goals. The richness of these applications, some of which are described in Part II, underscores the necessity of resolving problems that may hinder valuable TDR programs.

Fortunately, government operated TDR banks are able to lessen many of the described burdens, freeing TDRs to perform a critical function—the preservation of valuable public goods. Government operated TDR banks face some significant challenges, including the assertion that they may exacerbate strategic zoning and create a forum for government abuse of power. These concerns will be discussed in depth in Part III of this Note. First, however, it is helpful to examine several TDR schemes in practice.

II
Contemporary TDR Schemes and Their Use of TDR Banks

The following four programs illustrate the broad range of TDR applications in land use regulation as well as the effects that TDR banks are having on such schemes. New York City's South Street Seaport development, New Jersey's Pinelands preservation program, Seattle's low-income housing and landmark preservation programs, and Montgomery County's farmland preservation program represent four very different land use programs.

New York City's South Street Seaport project was a city administered program applied to one discrete district.[97] Seattle, similarly, represents a city government program, but one not limited to a single transfer and receiving district.[98] The New Jersey Pinelands, in contrast, illustrates a TDR scheme inspired by federal government action and administered by the state government on a regional basis.[99]

96 Program parameters should be established by legislation when TDR schemes are enacted. Verification of program compliance by an administering agency, or a TDR bank, is thus a ministerial duty and does not involve discretion nor give rise to conflicts of interest. Verification would include ensuring that transfers were made only from designated transfer districts to designated receiving districts, landowners sold no more TDRs than they were granted, and transfers did not exceed the maximum allowed per receiving property.

97 See infra Part II.A.

98 See infra Part II.B.

99 See infra Part II.C.

Montgomery County's program is run by a county government and has county-wide applications.[100] These four programs represent TDR programs and banks operated by different levels and forms of government with different sources of authority. They illustrate small, medium, and large programs, both urban and rural. Each program also demonstrates the efficacy of a TDR bank, which, in each case, was established explicitly to counter problems inherent in the use of TDRs. These problems varied, from valuation difficulties to timing gaps, but were all resolved by the creation of a TDR bank.

A. *New York's South Street Seaport Historic District*

In 1972 New York City, in its first area-wide TDR program, created a special South Street Seaport District[101] to preserve several blocks of small, two-hundred-year-old buildings surrounding the Fulton Street Fish Market, located directly south of the Brooklyn Bridge.[102] At that time the area was ripe for development because of high land values in Manhattan. The area also presented a historic area worthy of preservation.[103] In order to accomplish both preservation and development goals, the City created a special district containing both a preservation area and a redevelopment area.[104] Owners of historic properties in the preservation area were permitted to convey their development rights to a middleman or directly to a receiving lot in the redevelopment area.[105]

The middleman in this program was a consortium of commercial banks that held mortgages on the historic buildings and served as a TDR bank.[106] A middleman was necessary to facilitate the City's plan because the historic buildings were in need of immediate financial relief and extensive rehabilitation,[107] but direct transfers were unlikely to take place right away. This is because the designated receiving lots were limited to a relatively small redevelopment area, and direct transfer of the development rights could not take place until a property owner in that area was ready to develop.[108] Property owners that were ready at the outset of the program bought TDRs directly; those that were not purchased at a later date from the TDR bank.[109] Own-

100 See infra Part II.D.
101 See New York, N.Y., Zoning Res. ch. 8, §§ 88-00 to -08 (1998).
102 See id. § 88-03 and app. A, Transfer District Map.
103 See id. § 88-00; New York City Planning Comm'n, Report CP-21962 (1972).
104 See New York, N.Y., Zoning Res. ch. 8, §§ 88-00(d), 88-02 (1998).
105 See id. § 88-04 (1972).
106 See Marcus, Air Rights in New York City, supra note 9, at 891-92.
107 See id. at 892.
108 See Pedowitz, supra note 9, at 266.
109 See id.; Richards, supra note 9, at 465 n.97.

ers of historic buildings who were not able to sell their TDRs directly to receiving lots transferred them to the TDR bank. Individual banks in the consortium then released the mortgage indebtedness on the old buildings.[110] In essence, the banks exchanged mortgage debt for TDRs. Freeing owners of the landmark buildings from mortgage debt enabled them to attract substantial reinvestment financing, which they then used to restore the buildings.[111] When the banks later sold the development rights, they more than recouped the mortgage debt they had forgiven at the outset.[112] Development rights sold for significant amounts of money,[113] making the exchange profitable for the banks. The use of TDRs and the TDR bank benefited the district by facilitating the preservation of the Seaport's Schermerhorn Row landmark buildings and simultaneously encouraging the development of valuable land in the adjacent South Street Seaport commercial area.[114]

The South Street Seaport TDR program is currently, in effect, inactive. TDRs are no longer being granted in the historic district, and development in the adjacent development area has slowed.[115] TDRs remain available for sale by the bank, but it is unlikely that they will be purchased.[116] The consortium of banks made a profit on the TDRs they did sell,[117] however, and the program accomplished its goals of renovating and developing two finite districts within a particular time period.[118] Thus, the South Street Seaport TDR program was

[110] See Marcus, Air Rights in New York City, supra note 9, at 890-91.

[111] See id. at 891-92.

[112] See Telephone Interview with Phil Schneider, New York City Planning Department (Mar. 23, 1998) (noting that approximately 60% of TDRs have been sold).

[113] See Marcus, Air Rights in New York City, supra note 9, at 891 (describing one purchase of 300,000 square feet of development rights for $1,500,000); Richards, supra note 9, at 463 (describing purchase of 1.6 million square feet for $1,350,000, or approximately $4.40 per square foot).

[114] See Marcus, supra note 9, at 892. See generally New York City Planning Comm'n, Report CP-21962 (1972) (stating goals of South Street Seaport TDR program).

[115] See Telephone Interview with Phil Schneider, supra note 112.

[116] Approximately 500,000 square feet worth of TDRs remain in the TDR bank (held by Chase, the lead bank in the consortium). See id.

[117] Three major transactions took place under the South Street Seaport TDR scheme: Continental Corporation bought approximately 300,000 square feet to enlarge its 35-story skyscraper; 175 Water Street purchased 286,000 square feet; and 199 Water Street purchased 275,000 square feet. See Marcus, Air Rights in New York City, supra note 9, at 891-92; Richards, supra note 9, at 463-65.

[118] One additional twist to this program was that development rights were convertible into both increased tower coverage and floor area ratio rather than only floor area ratio. See New York, N.Y., Zoning Res. ch. 8, §§ 88-05, -06 (1998); see also supra note 25 for a definition of both FAR and tower coverage. A tower coverage waiver permits larger floors and leads to lower buildings that cover a greater percentage of the building lot, whereas FAR increases tend to result in taller buildings. In New York both tower coverage and FAR are strictly zoned, along with height and setback restrictions, so that increases in both can be extremely valuable. Allowing a combination of the two development types, as op-

a success; many valuable historic buildings were preserved, and the development area is now a thriving tourist center.[119]

B. *The New Jersey Pinelands Preservation Act*

In 1978 Congress established the Pinelands National Reserve, declaring a national interest in protecting and preserving approximately one million acres of pine-oak forest in southern New Jersey.[120] In its first application of the national reserve concept,[121] Congress not only declared a national interest in preserving the Pinelands but also elaborated many specific actions which should be taken by New Jersey.[122] The federal statute called for the development and implementation of a comprehensive plan,[123] a coordinated effort involving both the federal and state governments,[124] and provided for a range of technical[125] and financial support to assist New Jersey in the acquisition of property.[126] The federal government also recommended the study of a de-

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posed to simply allowing an increase in FAR, was expected to result in lower buildings and a net decrease in zoned density in the neighborhood. See New York City Planning Comm'n, Report N 810597 ZRM, 3 (1981) ("[T]he city achieves a reduction of density impacts associated with additional floor area at the expense of permitting increased tower coverage."). In order to maximize this benefit, the City amended its zoning resolution to increase the allowable tower coverage from 55% to 80% under the South Street Seaport TDR program. See id. at 2.

119 See Marcus, Air Rights in New York City, supra note 9, at 892.

120 See National Parks and Recreation Act of 1978, Pub. L. No. 95-625, tit. V, § 502, 92 Stat. 3492 (1978) (codified as amended at 16 U.S.C. § 471i (1994)). The Pinelands protect the Cohansey aquifer which contains more than 17 trillion gallons of potable water and shelters 580 native plant species, 299 bird species, 91 kinds of fish, 59 types of reptiles, and 39 species of mammals. The ecosystem also supports New Jersey's blueberry and cranberry industries, respectively the second and third largest in the nation. See Dana Clark & David Downes, What Price Biodiversity? Economic Incentives and Biodiversity Conversion in the United States, 11 J. Envtl. L. & Litig. 9, 53 (1996); see also N.J. Senate Energy & Env. Comm. Statement, S. No. 3091 (1991), reprinted in N.J. Stat. Ann. § 13:18A-1 (West 1997) (noting region's "significant and unique ecological, historical, recreational, and other resources").

121 See N.J. Senate Energy & Env. Comm. Statement, supra note 120 (explaining national reserve concept as new alternative to outright federal acquisition and management, which implements cooperative program involving federal, state, and local governments, private groups, and individuals).

122 See National Parks and Recreation Act of 1978, Pub. L. No. 95-625, tit. V, § 502, 92 Stat. 3492 (codified as amended at 16 U.S.C. § 471i (1994)).

123 See id. § 471i(d).

124 See id. §§ 471i(f)(4), (g)(2)(c).

125 See id. § 471i(g)(6).

126 See id. §§ 471i(h), (k). Congress appropriated $26,000,000, with a minimum of $23,000,000 for acquisition, and any of the additional $3,000,000 not used for planning to go to acquisition as well. In addition, up to $14,500,000 was made available in matching funds (with state to provide 50% or more) for land acquisition. The legislation prioritized certain areas in which purchase should take place. See id. § 471i(k).

velopment credit bank,[127] which ultimately led to the creation of the Pinelands Development Credit Bank.[128] The New Jersey legislature enacted the Pinelands Protection Act[129] to implement the provisions of the federal act. Among other things, the Act established the Pinelands Commission and directed that it prepare a comprehensive management plan (CMP) for the Pinelands.[130] The CMP, which was drafted and approved in 1981,[131] established a TDR program for New Jersey.[132]

The TDR scheme calls for granting Pineland Development Credits (PDCs), or TDRs, to owners in protected areas, which can be purchased by landowners wanting to increase construction density in regional growth areas, and to a more limited extent in rural development areas.[133] Landowners selling PDCs retain title to the land and may continue using it for authorized, nonresidential purposes. Prior to the sale of credits, a landowner must record a deed restriction binding all subsequent owners of the land to uses that conform with the Pinelands comprehensive management plan.[134]

In order to realize the "full measure of the benefits" of its TDR program, the New Jersey legislature found that "steps must be taken to assure the marketability of [the] credits."[135] It concluded that the best means of providing this assurance was by establishing a TDR bank. The Pinelands Development Credit Bank was created by the New Jersey legislature in 1985, and is authorized to act as the buyer of

127 See id. § 471i(l).

128 See N.J. Stat. Ann. § 13:18A-31 (West 1997).

129 N.J. Stat. Ann. § 13:18A (West 1997).

130 See id. § 13:18A-8.

131 See id. § 13:18A-10.

132 The Pinelands were divided into eight land use zones. The most ecologically sensitive areas were classified as Preservation Areas, in which most residential, commercial, and industrial development is prohibited. Some activities, such as forestry and recreational uses, as well as berry and native plant harvesting, are allowed if in conformance with environmental standards. See Clark & Downes, supra note 120, at 53. Protection Areas were created where growth is encouraged, subject to environmental and zoning standards, but only up to a predetermined density. These include Forest Areas, Agricultural Production Areas, Regional Growth Areas, and Rural Development Areas. The Commission determined the number of new housing units that could be accommodated and distributed them throughout the Regional Growth Areas. In order to reduce the development pressure on the Regional Growth Areas, Rural Development Areas are treated as transition zones where modest development is allowed. See id. at 54.

133 PDCs may not be transferred outside of designated Pinelands districts, to other parts of New Jersey, for example, but may be transferred across municipal and county boundaries within the Pinelands region. See Telephone Interview with John Ross, supra note 90.

134 See N.J. Stat. Ann. § 13:18A-35 (West 1997).

135 Id. § 13:18A-31.

"last resort"[136] for development credits as well as to guarantee loans secured by PDCs.[137] The bank is mandated to purchase or guarantee the value of a PDC for a minimum price.[138] The guarantee of loans secured by PDCs is simply another way that the bank ensures the value of PDCs, encouraging their treatment as an actual asset, like real property. Property owners in restricted development areas may use their PDCs as collateral, so that even without sale the PDCs have value. If a default occurs, the bank pays the loan and takes the PDC.

The bank is authorized to purchase PDCs only when necessary to further the objectives of the comprehensive plan or when necessary to alleviate hardship to a landowner.[139] Legislation set a minimum price of $10,000 per credit, which the board of the bank may increase or decrease, "provided that its action does not substantially impair the private sale" of PDCs.[140] To assure that private sale remains the most desirable method of exchange, the bank may never pay more than 80% of market value for PDCs.[141] The bank may sell any PDCs it acquires or it may apply them at no cost for use in projects that "satisfy a compelling public purpose."[142]

Another essential function of the bank is to maintain a registry of PDCs, which keeps track of all PDCs assigned, records who buys and sells PDCs, records who pledges a PDC as security for a loan, and compiles annual numbers of all PDCs transferred in each locality which it makes available to the public annually.[143]

New Jersey's legislature established the Pinelands Development Bank "as an instrumentality of the State" that serves a purpose "deemed and held to be an essential governmental function of the

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136 See N.J. Senate Land Use Management & Regional Affairs Comm'n Statement, S. No. 2462 (1991), reprinted in N.J. Stat. Ann. § 13:18A-48 (West 1991) ("The bank acts as a 'last resort' purchaser of such credits when a seller is unable to find a private buyer."); N.J. Senate Finance & Appropriations Comm'n Statement, S. No. 1945 (1985), reprinted in N.J. Stat. Ann. § 13:18A-30 (West 1991) ("The board [of directors for the Pinelands Development Credit Bank] is further authorized to act as a last resort buyer of development credits in the event of economic hardship or to further the purposes of the 'Pinelands Protection Act' . . . .").

137 See N.J. Stat. Ann. § 13:18A-38 (West 1997).

138 See id. §§ 13:18A-34(g), 18A-39 (setting minimum price for PDCs at $10,000).

139 See id. § 13:18A-34(g).

140 Id. This minimum price has been raised to $12,600. See Telephone Interview with John Ross, supra note 90.

141 See N.J. Stat. Ann. § 13:18A-34(g) (West 1997). The minimum amount paid may be adjusted by the Board if 80% of market price were ever to drop below this minimum price, so the 80% cap does not conflict with the minimum value requirement. Currently, this is not a concern, as market price and the minimum amount paid are both increasing. See Telephone Interview with John Ross, supra note 90.

142 N.J. Stat. Ann. § 13:18A-42 (West 1997).

143 See id. § 13:18A-36.

State."[144] The legislature appropriated five million dollars of state funds for the purchase of PDCs, and to extend PDC guarantees. The State limited the bank's operations, however, and required all money on deposit to be transferred to the General Fund at the end of fifteen years.[145] It also set an expiration date of December 31, 1990 on the bank's ability to buy, sell, and guarantee PDCs.[146] This date was later extended to 1992,[147] and again until 2005, because it was determined that the bank is serving an essential function.[148] After this period, the bank is authorized to facilitate transfers between private parties and to continue its registry of PDCs, but it may no longer act as a market participant.[149] It appears that the New Jersey legislature recognized the initial need for a TDR bank to guarantee a market and value for the PDCs, but was concerned about long term interference with the private sale of PDCs.[150]

Thus far, PDCs are being purchased predominantly in the private market, although the bank is involved in every PDC transaction to some extent due to its role as the registry, the issuer of PDC certificates, and the recorder of all transfers.[151] No landowner has yet exercised the option to use PDCs to secure a bank loan,[152] and the bank has purchased PDCs very infrequently.[153] Nonetheless, program administrators consider the bank to be very successful in its role as coordinator, monitor, and facilitator of PDC transactions.[154]

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[144] Id. § 13:18A-33.

[145] See id. § 13:18A-47; see also N.J. Senate Finance & Appropriations Comm. Statement, S. No. 1945 (1985), reprinted in N.J. Stat. Ann. § 13:18A-30 (West 1991) (appropriating $5,000,000 from General Fund to capitalize Bank, but requiring reversion of any remaining funds after 15 years).

[146] See N.J. Stat. Ann. § 13:18A-47 (West 1997).

[147] See id. § 13:18A-48 (extending bank's operations to allow for five full years).

[148] See Telephone Interview with John Ross, supra note 90 (attributing bank's extended operations to its success, stating that bank "simplifies the process" for participants by helping buyers find sellers and helping sellers understand the program).

[149] See N.J. Senate Land Use Management & Regional Affairs Comm. Statement, S. No. 2462 (1991), reprinted in N.J. Stat. Ann. § 13:18A-48 (West 1991) (stating that after expiration period bank will not have authority to buy, sell, or guarantee loans for PDCs).

[150] See, e.g., N.J. Stat. Ann. § 13:18A-34(g) (West 1997) (authorizing bank to "periodically increase the purchase price [of PDCs]; provided that its action does not substantially impair the private sale of pinelands development credits").

[151] See Telephone Interview with John Ross, supra note 90 (stating that buyers can contact sellers directly, but usually go to bank for lists of sellers because it is easier). The rate of sales for PDCs has increased since the bank began operating; in the past three years PDCs have been selling at a rate of approximately 150 per year. See id.

[152] See id. (stating that no one has used loan guarantee option, but it remains in place "if need be").

[153] See id. (stating that bank's main role is administrator/facilitator of program and is only buyer of last resort).

[154] See id. (stating that whether it is called a clearinghouse or a bank, the role it serves is very important; TDR bank is "key element in any TDR program").

C. Seattle's Downtown Transferable Development Rights Program

Seattle's downtown land use code has, for some time, included a TDR mechanism in conjunction with the City's Housing Bonus Program.[155] This program allows development rights from low-income buildings to be sold and transferred to commercial developers in most downtown zones.[156] The purpose of this program is to preserve low-income housing sites by reducing economic incentives to replace properties in valuable downtown areas with more profitable commercial development.[157] Under Seattle's original TDR program, the transfer of development rights had to be simultaneous, meaning that there had to be a private buyer before the TDRs could be sold.[158] This requirement, along with a variety of other factors, kept the production and preservation of low-income housing relatively low.[159]

In 1988 Seattle passed a new ordinance authorizing the creation of a TDR bank to overcome some of the obstacles inherent in its TDR program.[160] Identifying the "timing gap" as one of the most significant problems, the City of Seattle Department of Community Development (DCD) recommended establishment of a TDR bank.[161] Such a bank would enable the City to buy development rights from residential buildings, hold them in the bank, and sell them to developers seeking additional density for new commercial projects. The DCD anticipated that demand for TDRs would follow their purchase date by five to seven years.[162] By supplying a holding entity for TDRs, the City planned to fill the "timing gap" and increase the amount of low-income housing preserved.[163] The City adopted the DCD's recommendations and established a bank to purchase TDRs from low-income residential structures in downtown zones, hold them for such periods as necessary, and then sell them to qualified developers.[164]

155 See City of Seattle Dep't of Community Dev. & Downtown Hous. Advisory Task Force, Transfer Development Rights TDR Bank Report 1 (May 1988), passed into law as Seattle, Wash., Ordinance 114029 (June 27, 1988) [hereinafter TDR Bank Report] (describing the use and purpose of TDRs in Seattle).

156 See id.

157 See id.

158 See id.

159 See id. (naming slowdown in commercial development as factor in low production and preservation rates of low-income housing).

160 See Seattle, Wash., Ordinance 114029 (June 27, 1988).

161 See TDR Bank Report, supra note 155, at 1.

162 See id.; see also Telephone Interview with Jane Voget, Senior Project Manager, City of Seattle Department of Housing and Human Services (June 17, 1998) (explaining that timing gap was identified by studying downtown development cycle).

163 See TDR Bank Report, supra note 155, at 1-2.

164 See id.

Initial City purchases of TDRs were through a twenty year Life Renovation Program.[165] The program was aimed at occupied, or recently vacant, properties that provide low-income housing.[166] When originally adopted, the program included a component that enabled the City to lease, purchase, or negotiate an option to buy development rights from low-income buildings rather than purchase the TDRs themselves, but this part of the program was never implemented.[167] Under current rules, TDRs may also be purchased from newly constructed low-income housing located in eligible downtown zones.[168]

The City funded the bank at $3.5 million for its first three years.[169] It was hoped that the TDR bank would facilitate the long term preservation of an additional 100 units of low-income housing in downtown Seattle and reduce the development pressure on up to 250 units.[170] In fact, between 1985 and 1991 (the TDR bank was established in 1988), Seattle's TDR programs yielded 337 units of afforda-

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165 At time of passage, there were 36 occupied and 17 vacant buildings listed as eligible for TDR bank purchase. See id. at 5.

166 At least 51% of the occupants must be low-income, which is defined as 35% of 50% of area median income. See id. at 2. Properties qualify by satisfying a number of basic requirements, passing threshold criteria, and then competing with other properties for TDR Bank funds. Basic requirements include minimum low-income housing set asides; satisfaction of applicable building codes and standards; a minimum economic and functional building life of 20 years (as determined by DCD); financing necessary for rehabilitation (if financing is provided, it must be placed in escrow until rehabilitation is completed); and qualifying rent levels. See id. at 3-4. Threshold criteria are 1) that the project serve low-income people, with preference to very low-income persons, and 2) without the TDR purchase, the project would not be economically viable. See id. at 4-5. Competitive criteria include risk of loss due to demolition or change of use; secure project funding; high square footage of low-income housing per city dollar; affordability of rents; project viability; site; and availability and commitment of other funding sources. See id. Those buildings selected to sell their TDRs to the bank must commit to operate the property as low-income housing for at least 20 years. This commitment is executed through a regulatory agreement recorded as a covenant running with the land. See id. at 4.

167 See Telephone Interview with Jane Voget, supra note 162 (stating that Seattle never leased or purchased options on TDRs, but that it does include options to buy TDRs in loan agreements that City makes to low-income housing developers).

168 See id.

169 See TDR Bank Report, supra note 155, at 13. The City recognized that TDR sales provide only a portion of the costs of rehabilitation and operation of low-income housing and that the TDR Bank only increases the City's capacity to preserve downtown, low-income housing to the extent that other public funds are available for gap financing. Given the amount of other public funds available in 1988-89, for example, the City originally determined that it would be able to purchase two million dollars worth of TDRs. See id. at 6 for a more detailed example of this financial scenario. The funds allocated were later reduced to $1.25 million due to a lack of purchasing ability between 1988 and 1991.

170 See id. at intro. The cumulative goal for all City programs was to assist in preserving 7,311 low-income housing units in downtown Seattle. See id.

ble housing,[171] and has gone on to earn the City commendations for its innovative use of TDRs.[172]

In 1992 the City Council authorized the proceeds from the sale of TDRs and all other income from the TDR Bank Program to be deposited into the Low Income Housing Fund for future TDR purchases.[173] This established a self-sustaining TDR bank, rather than an entity reliant on annual budget allocations from the Cumulative Reserve Fund.

The success of the TDR bank in low-income housing preservation led the City Council, in 1993, to authorize the bank to purchase, lease, or acquire options on TDRs from landmark performing arts theaters as well.[174] This provided a mechanism for the rehabilitation and preservation of landmarked theaters in advance of the availability of a private TDR purchaser.[175]

171 See Theodore C. Taub, Update on Affordable Housing 853, 880 (ALI-ABA Course of Study Materials: Planning, Regulation, Litigation, Eminent Domain, and Compensation No. C629, 1991) (describing state and local programs designed to provide low-income housing).

172 See Telephone Interview with Jane Voget, supra note 162 (stating that Seattle's program won 1997 Puget Sound Regional Council Vision 20/20 Award for Innovative Achievement in Local Government).

173 See Seattle, Wash., Ordinance 116366 § 6 (Sept. 28, 1992). At the same time, the Council modified the TDR Bank Program to add new construction projects and vacant properties as classes of property eligible for TDR purchase under the 20-year Life Renovation Program. See id. § 4.

174 See Seattle, Wash., Ordinance 116513 § 1(G) (Jan. 4, 1993).

175 Owners of landmarked performing arts theaters, identified by the City Council as "unique and irreplaceable contribution[s] to the physical environment, culture and quality of life of the City," Seattle, Wash., Ordinance 116513 § 1(A) (Jan. 4, 1993), are now able to sell TDRs to the TDR bank if the sale is necessary to fill a financing gap for rehabilitation of the theater. See Seattle, Wash., Mun. Code § 23.49.033(B)(2)(a)(iii) (1998). A financing gap is the amount required to satisfactorily preserve and maintain a landmark, or low-income housing, less the "reasonable economic return" generated by the property. See id. An owner does not have to sell to the TDR Bank, and may sell to anyone, regardless of whether the purchaser is the owner of an eligible receiving lot, as long as the sale complies with program regulations. See id. § 23.49.033(E)(1). Upon sale of a TDR, an owner must agree to renovate and maintain the structure in compliance with Landmarks Board requirements for at least 40 years. Additionally, the building must remain, as its primary use, a performing arts theater. See id. § 23.49.052(D)(4). Sometimes the performing arts theaters are also sources of low-income housing. See Seattle, Wash., Ordinance 116513 § 1(F). When this is the case, an owner selling TDRs to the bank is required to preserve and maintain the units, or replace any low-income housing destroyed by the preservation of the theater, for a minimum of 20 years. See Seattle, Wash., Mun. Code §§ 23.49.072(D), 3.20.320(E).

A purchaser of landmark theater TDRs must provide security, or consideration, for the TDRs in an amount approved by the Director of Housing and Human Services. This amount is placed in escrow, as the seller of the TDRs is only entitled to receive payment upon completion of approved rehabilitation of the landmark. See Seattle, Wash., Mun. Code § 23.49.033(E)(2). If the owner fails to proceed with or complete the rehabilitation as required, the use of the TDR by the purchaser is not affected. Rather, the payment for

The amounts paid by the bank for TDRs are limited.[176] The amount paid by developers under the cash option for the Housing Bonus Program to the bank ranges from $13 to $20 per gross commercial square foot, depending on the zone in which the development is located.[177] In one well-publicized transaction, a four-star downtown hotel purchased 130,012 square feet, or ten additional building stories, from the City for $1.47 million.[178] Such sales fund the TDR Bank's continued operation, as well as additional development and preservation of low-income housing in the downtown area.[179]

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the TDRs shall then be made to the City to be used for the preservation of other landmarks. See id.

To date, two landmarked historic performing arts theaters have been preserved through the TDR Bank Program—the Eagles Auditorium and the Paramount Theatre. See Hotel OK'd to Build 25 Stories Now, Seattle Times, Oct. 1, 1996, at B2 (reporting sale of TDRs to developer of Seattle Hyatt Regency); Peter Lewis, Cole Threat: Paramount May Be Sold, Seattle Times, Oct. 22, 1996, at B1 (reporting conflict over renovation of Paramount Theatre and sale of its TDRs). In addition, the City, in conjunction with the Seattle Symphony, is building a brand new concert hall in downtown Seattle which is being partially funded by up to $5,000,000 in TDR proceeds. See Telephone Interview with Jane Voget, supra note 162; see also Ellen Pfeifer, Theater; Forum Focuses on Opera House, Theater Restoration, Boston Herald, Mar. 28, 1996, at 45, available in LEXIS, News Library, BHerld File (describing Seattle's use of TDRs to raise funds for new concert hall); Seattle Symphony Announces Design for Benaroya Hall, PR Newswire, Nov. 29, 1995, available in LEXIS, News Library, PRNews File (describing plans for new Seattle Symphony concert hall).

176 The City determines the price it pays for TDRs by engaging in a "subsidy review," starting with the appraised value of the TDRs and then reducing the price of the TDRs, or the number purchased, so that Seattle only pays the equivalent of the property's financing gap. By paying only what the financing gap demands, Seattle ensures that owners do not receive an excess subsidy. See Telephone Interview with Jane Voget, supra note 162.

177 See Taub, supra note 171, at 880 (describing developers purchase of density bonuses in Seattle); see also Telephone Interview with Jane Voget, supra note 162.

178 See Hotel OK'd to Build 25 Stories Now, supra note 175, at B2 (describing Seattle City Council authorization of TDR sale to developer of Seattle Hyatt Regency); Nat'l Mortgage News, Sept. 8, 1997, at 46, available in LEXIS, News Library, NMN File (describing Starwood Lodging Trust's purchase of $1.5 million of TDRs); Starwood Lodging Begins Construction of 426-Room Upscale Hotel in Downtown Seattle, Bus. Wire, Aug. 21, 1997, available in LEXIS, News Library, Bwire File (reporting construction of first full-service hotel built in Seattle since 1983).

179 Seattle's TDR scheme is complicated by the fact that it is intertwined with a public benefits bonus scheme that allows developers additional rights (i.e., FAR) for provision of specified public benefits. See, e.g., Table of Public Benefit Feature Area Bonuses, Seattle, Wash., Mun. Code § 23.49.050 B (as amended by Seattle, Wash., Ordinance 116513 (Jan. 4, 1993)). Because the City is encouraging the preservation of low-income housing, landmarks, and the creation of public benefits through many incentive programs, it has established a complex procedure for ensuring prioritization of certain public goods. See, e.g., Seattle, Wash., Ordinance 116513 § 3(B) (Jan. 4, 1993) (giving TDRs from landmark performing arts theaters priority over any other landmark TDRs); id. § 8(B)(1)(b) (prohibiting transfers of low-income housing TDRs in certain downtown areas until the receiving lot has provided enough public benefit features to double its FAR). Seattle has created a maze of incentives in an attempt to encourage the creation of multiple public goods. For a

D. Montgomery County's Farmland Preservation Program

State and local governments throughout the nation have begun to acknowledge a real threat to agricultural land uses.[180] Farmland near cities is becoming highly attractive to people who want to live outside of a city but near enough to commute to work, and subdivisions are replacing once active farms.[181] This demand is causing rural land prices to rise beyond their use value in agriculture.[182] Much as downtown land prices make development more profitable than preservation, rapidly rising agricultural land prices often make selling to a subdivision far more profitable than running a farm.[183] Because few purchasers continue to operate farms, the concern over loss of farmland is more than an aesthetic or cultural concern—localities are beginning to worry about the loss of farm products.[184]

In 1956 Maryland was the first state to take action to halt this trend, when its legislature enacted a law to provide preferential tax assessments on farmland to encourage farmers not to sell to developers.[185] Today, Maryland continues to protect farmland, as exhibited by Montgomery County's adoption of a plan to preserve agriculture and rural open space. The County's General Plan, adopted in 1964, declared the prevention of urbanization of open spaces as one of its planning purposes but left the development of a detailed implementation strategy to a later date.[186] The implementation strategy subsequently developed in Montgomery County's Functional Master Plan

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discussion of competing incentive programs and their impact on TDR use, see Richards, supra note 9, at 474-79.

180 As of late 1980, 42 states had enacted legislation providing preferential tax assessments on farmland in the hope of encouraging farmers not to sell their property. See Maryland-National Capital Park & Planning Commission, Series No. 0656802506, Functional Master Plan for the Preservation of Agriculture and Rural Open Space in Montgomery County 1 (Oct. 1980) (approved and adopted Sept. 30, 1980) [hereinafter Functional Master Plan]. But see William A. Fischel, The Economics of Zoning Laws: A Property Rights Approach to American Land Use Controls 273-92 (1985) (arguing that there is no shortage of agricultural land in United States).

181 See Functional Master Plan, supra note 180, at 10.

182 See id. at 12 (documenting jump in land prices in Montgomery County from $700 per acre in 1959 to $3,500 per acre in 1979).

183 Many factors, including "development pressures, rising taxes, departure of support industry for stronger markets, loss of political influence, laws that inhibit necessary agricultural practices, rising labor costs in the face of urban employment opportunities, suburban neighbor nuisances, and land speculation," converge to make it very difficult for farmers to refuse tempting offers to sell. Id. at 11.

184 See Rene Johnson, The Consequences of No Preservation Effort 3 (Montgomery County Office of Economic and Agricultural Development, Apr. 1979) (stating that purchasers usually have "little intention of contributing to the farm product market") (quoted in Functional Master Plan, supra note 180, at 10).

185 See Functional Master Plan, supra note 180, at 1.

186 See id. at 3-4.

(the Plan) included a TDR program and bank, and was adopted in 1980.[187]

The Plan combines use of the State Agricultural Land Preservation Program, rural cluster zoning, and the transfer of development rights from Agricultural Reserve areas to Rural Density Transfer Zones and Growth Centers along major transportation corridors.[188] All zoning changes were implemented through comprehensive rezoning.[189] The Plan is "based upon the assumption[s] that [farmland] preservation is in the public interest" and that local government plays a "critical role" in the protection of that interest.[190] The County identifies and attributes cultural and historic value, environmental value in the management of soil, water, and air resources, and regional economic value to farmland.[191] The goal of the Plan is to preserve 110,000 acres of Agricultural Reserve and 26,000 acres of Rural Open Space.[192]

The TDR program includes many of the same design guidelines as the New Jersey Pinelands program.[193] TDRs are granted to landowners in Agricultural Reserve areas in exchange for restrictive easements which permanently limit development of the property.[194] The landowner may then sell the TDRs to a developer in a designated receiving area. All sales must be recorded with the County.[195] A landowner may elect to develop his land but may only do so at a base density of one dwelling unit per twenty-five acres. In the alternative, he may also elect to sell the TDRs to a developer based on a density of one dwelling unit per five acres.[196] This sets up a voluntary TDR program with incentive bonuses that encourage transfer rather than development.

Although the Plan issued TDRs immediately, it did not simultaneously identify receiving areas for the TDRs. Rather, it ordered a

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187 The Functional Master Plan was approved by the Montgomery County Council, sitting as the District Council, by Resolution No. 9-979, and by the Maryland-National Capital Park and Planning Commission by Resolution No. 80-26, in September of 1980. See id. at Certificate of Approval & Adoption.

188 See id. at 32-48.

189 See id. at 8.

190 Id. at 34.

191 See id. at 21, 34 (explaining that farm products account for approximately $23,000,000 of County's 1979 total gross productivity).

192 See id. at 39.

193 See Tripp & Dudek, supra note 9, at 382 n.36.

194 See Functional Master Plan, supra note 180, at 87-88 (quoting Montgomery County, Md., Zoning Ordinance § 59-A-6.1 (1980)).

195 See id. at 87 (quoting Montgomery County, Md., Zoning Ordinance § 59-A-6.1(b) (1980)).

196 See Functional Master Plan, supra note 180, at 43; id. at 87 (quoting Montgomery County, Md., Zoning Ordinance §§ 59-A-6.1(c), (d) (1980)).

detailed study of the region to identify receiving areas where increased density would present minimal adverse community impact, and where density bonuses would be valuable enough to provide a healthy market for the TDRs.[197] The Plan called for the completion of the study within two years.[198] In order to allow purchase of TDRs prior to the designation of receiving areas, the Plan called for the creation of a County Development Rights Fund (a TDR bank).[199] The bank was funded by general obligation bonds and operated by the County government.[200] It ensured an interim market for TDRs by guaranteeing loans secured by TDRs through private banks, by making loans to farmers using TDRs as collateral, and by directly purchasing the TDRs itself.[201] If TDRs were purchased, the bank was authorized to hold them until appropriate receiving areas were identified, liquidate its holdings, and then return the proceeds to the County treasury. As the Plan recognized, "[t]he Fund [was] a critical element to the success of the proposed farmland preservation program."[202]

In fact, the bank remained in operation from 1982 until 1990, when the legislation authorizing its existence was allowed to sunset.[203] Approximately 18,000 TDRs were issued in 1980, but the first receiving areas for the TDRs were identified in 1982 and accommodated only 3,200 TDRs.[204] The bank was needed, therefore, to fill the timing gap between the issuance of TDRs and the identification of receiving areas.[205] Montgomery County continues to identify receiving areas, to assure farmland owners an adequate market for their TDRs, but it no longer needs a bank to guarantee a purchaser.[206] Although the bank was budgeted two million dollars to secure loans or purchase TDRs, the bank was never used for this purpose.[207] The private mar-

197 See Functional Master Plan, supra note 180, at 44 (describing need for detailed study of receiving areas).

198 See id.

199 See id. ("The proposed County Development Rights Fund could play an important role in development right purchase prior to the opening of appropriate receiving areas.").

200 See id. at 47.

201 See id.

202 Id. at 48.

203 See Telephone Interview with Denis Canavan, Zoning Coordinator, Montgomery County, Maryland (Mar. 26, 1998).

204 See id.

205 See id.; see also Eugene L. Meyer, Saving Farmland: Citizens Oppose County Plan to Preserve Its Open Spaces, Wash. Post, July 7, 1982, at C1 (describing landowners' discontent and lawsuit claiming devaluation of property because no market existed for TDRs, which was "widely regarded as a prod to get the county to . . . fulfill its promise to create a 'Development Rights Bank' to buy TDRs until a substantial private market" was established).

206 See Telephone Interview with Denis Canavan, supra note 203.

207 See id. (stating that bank did not receive any applications for purchase of TDRs).

ket was strong enough to support all purchases of TDRs, shifting the bank's role from guarantor of TDRs to that of assuring the "credibility" of the program.[208] When designed, Montgomery County's program assumed that a private market would develop for TDRs, but until borne out in practice, this assumption was tentative.[209] The bank served an important role, inspiring confidence in the program until it became certain that TDRs would have private market value.[210] While the bank was in operation, Montgomery County preserved nearly 27,000 acres of farmland.[211]

III
A Critical Analysis of TDR Banks

Government operated TDR banks raise a host of legal and financial concerns. Within these two broader categories, there appear to be six primary areas of concern: strategic zoning challenges, antitrust challenges, authority challenges, legitimate public purpose requirements, municipal revenue problems, and valuation difficulties. For ease of treatment, this Part will address each of these issues separately, although in practice many of the categories are interrelated and coexist, exacerbating the problems that they pose individually. Legal issues will be addressed in Part III.A and financial issues in Part III.B.

A. *Legal Issues Facing TDR Banks*

The four issues addressed in this section are strategic zoning challenges, antitrust challenges, authority challenges, and the legitimate public purpose requirement. These issues are not new to municipalities or local governments, as they are similar to concerns that arise in connection with the traditional exercise of police power.[212] Because TDR banks are relatively new, and present some variations on the accepted governmental exercise of police power, they may be subjected to challenges on these grounds. Although none of the pro-

[208] See id. (attributing strength of private market to high demand for housing in Montgomery County, and stating that bank's purpose shifted from buyer of last resort to provider of "confidence" in program).

[209] See id. (stating that bank was "necessary" and "confidence factor" was important until success of TDRs in private market was proven).

[210] See id.

[211] See Tripp & Dudek, supra note 9, at 382 n.36 (citing telephone interview with Melissa Banach, Chief of Community Planning, North Division, Maryland-National Capital Park & Planning Comm'n (Feb. 8, 1989)).

[212] Police power is conferred to states by the Tenth Amendment and is, in turn, delegated to local governments to adopt such regulations as necessary to further legitimate public purposes, such as promotion of health, safety, morals, and general welfare, within the confines of constitutionally required due process. See U.S. Const. amends. X, XIV.

grams examined in Part II faced such challenges to their TDR banks, the success of these programs and a growing interest in the use of banks to facilitate preservation programs has lead more localities to create, or consider creating, TDR banks.[213] Widespread enactment of TDR banks may give rise to increased resistance to their use.[214] Local governments that utilize TDR banks must therefore take the following issues into consideration when establishing TDR banks.

1. *Strategic Zoning*

Perhaps the greatest challenge facing TDR banks is the exacerbation of an elemental problem of TDRs themselves—strategic zoning.[215] When governments utilize TDR schemes they often have incentives to underzone certain areas in order to create a market for the TDRs they are granting in others. Without a market, TDRs are worthless and will not be acceptable as compensation for restricted property rights. The government may then lose its ability to restrict development in preservation areas through regulation, forcing it to use valuable tax revenues to purchase development rights or forego preservation efforts. Thus, the government has strong incentives to restrict development in areas anticipated to receive TDRs. These incentives are only magnified when the government is also the bank which stands to profit from the sale of TDRs.

A strategic zoning challenge asserts that landowners' substantive due process has been violated.[216] If successful, such a challenge may invalidate the zoning scheme itself. It is, however, more likely to result in a determination that private property *in the receiving district* has been taken without just compensation, because owners of underzoned property will have lost economic value.

213 See, e.g., Roger K. Lewis, Little-Used Zoning Strategy Could Keep Suburban Sprawl in Check, Wash. Post, Nov. 16, 1996, at E1 (describing potential of TDRs to meet land use needs, and TDR banks to facilitate TDR programs that, "in the next century, . . . [are] sure to become one of the most powerful growth management tools").

214 This resistance may come from landowners subjected to development restrictions, private entities that would like to monopolize or control the TDR market, or individuals who object to certain land use regulations and are looking for ways to invalidate a TDR program.

215 See, e.g., Kayden, supra note 9, at 571-72 (addressing "baseline" property rights issue and possibility that "governments cynically . . . manipulate the baseline, tightening regulation beyond what otherwise would be appropriate").

216 The doctrine of substantive due process is derived from the Fifth and Fourteenth Amendments to the U.S. Constitution and requires legislation to be fair and reasonable in content as well as application. "The essence of substantive due process is protection from arbitrary and unreasonable action." Black's Law Dictionary 1429 (6th ed. 1990).

Governments must therefore balance the risk of overdensification or overbuilding against the problems created by underzoning.[217] For example, if all areas of a city are zoned to allow the greatest development reasonable (considering factors such as the capacity of municipal services, geographic/topographic factors, health, welfare, and safety), then the transfer of additional development rights will result in overdensification.[218] If certain "transferee districts" are zoned to allow less development in anticipation of TDRs, then landowners in that district will lose value. Either way, comprehensive planning may be called into question, and the government may be vulnerable to charges that its dual zoning scheme is arbitrary.

Costonis addressed this challenge by stating that it "fundamentally misconceives the process by which . . . [zoning is] determined and the functions that [it serves]."[219] He asserted that zoning determinations are made "on at least two levels: fact determination and political judgment."[220] The factors that determine appropriate zoning levels, such as regulating population, insuring adequate light, air, and open space, and avoiding excessive demands on public services, may be projected on a tentative basis at best.[221] Costonis argued that political judgments remain at the crux of zoning decisions.[222] Because there are no precise calculations that dictate "correct" zoning, the best that can be hoped for is a range of reasonable development.[223] Costonis asserted that density increases permitted under a TDR scheme should be seen not as arbitrary or strategic zoning, but as increments falling within a reasonable range of allowable development.[224]

Costonis's explanation provides some assurance that substantive due process concerns may not invalidate a reasonable TDR banking scheme.[225] It does not, however, directly respond to fears that local governments may zone strategically in order to raise the value of

217 See, e.g., Costonis, The Chicago Plan, supra note 9, at 598 ("The problem here is to strike a correct balance between preventing urban design abuse through proper planning controls and facilitating the marketability of development rights . . . .").

218 See, e.g., Meyer, supra note 19, at C1 (describing opposition of residents angered by threat of increased density in designated receiving districts in Montgomery County, Maryland).

219 Costonis, The Chicago Plan, supra note 9, at 628-29.

220 Id. at 629.

221 See id. (stating that "[t]he facts that must be established or projected . . . are often elusive and inevitably tentative").

222 See id.

223 See id. at 630.

224 See id. at 629-31.

225 If a government entity can point to evidence that its action was not arbitrary, but was reasonable in light of health, safety, and general welfare concerns, it is likely that a court will defer to the government's judgment. See infra Part III.A.4.

TDRs, and then profit from their position as bankers. Norman Marcus, former General Counsel of the New York City Planning Commission, goes so far as to call this situation "zoning for sale."[226] A slightly different twist on this scenario is what Marcus describes as the government's "schizoid dual role."[227] He is referring to the government's role as entrepreneur, interested in increasing public funds by selling development rights at the highest price possible, and its conflicting duty as the police power charged with minimizing overbuilding that might result from the sale of TDRs. In both cases, the government is serving the interests of the public, but becomes subject to conflicting demands when it attempts to fill multiple roles.

Despite frequently expressed concerns of this kind, no empirical evidence has been assembled which substantiates the fear that governments are engaging in strategic zoning. Jerold S. Kayden, Senior Fellow at the Lincoln Institute of Land Policy, writes that the strategic zoning scenario appears unlikely in areas where incentive zoning bonuses or TDRs have been added to existing zoning plans.[228] He acknowledges that when bonuses arise in the context of a complete overhaul of the zoning ordinance, strategic zoning is a more legitimate fear. Even then, however, he finds the charge to be "hardly overpowering."[229]

Testing for strategic zoning is difficult; a lack of empirical evidence does not necessarily mean that strategic zoning is not taking place. One action that should trigger suspicion is a zoning change which reduces allowable development in an area that is also designated as a receiving district for TDRs. This effect, reduced development in a receiving district, should be suspect whether the zoning takes place before, simultaneously, or after designation as a receiving district.[230] Local government should take precautions to ensure that

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226 See Marcus, Transferable Development Rights, supra note 9, at 41.

227 See id.

228 See Kayden, supra note 9, at 571-72.

229 See id. at 572 ("To the extent that bonuses arise in the context of a complete overhaul of a city's zoning ordinance, the charge [of strategic zoning] acquires greater, although hardly overpowering, resonance.").

230 Unfortunately, gradual or small-scale zoning changes are difficult to identify. Courts are likely to view this kind of change as weak evidence of strategic zoning, due to the high level of deference granted to government zoning decisions. Government regulations, if buttressed by a valid public purpose, are granted great deference, even in the face of illegal behavior. See, e.g., City of Columbia v. Omni Outdoor Adver., Inc., 499 U.S. 365, 378 (1991):

> [U]nlawful activity has no necessary relationship to whether the governmental action is in the public interest.... When, moreover, the regulatory body is not a single individual but a state legislature or city council, there is even less reason to believe that violation of the law ... establishes that the regulation has no valid public purpose.

strategic zoning challenges do not undermine the efficacy of their TDR programs.

While strategic zoning remains a possibility, it is not necessarily an inevitable prerequisite for a successful TDR program. There is no evidence of strategic zoning taking place in any of the TDR programs examined in this Note, and no legal challenges asserting as much have been filed. Because the opportunity for government misbehavior increases with the amount of discretion allowed, TDR schemes in which the government plays multiple roles are especially susceptible to abuse and should integrate checks on this kind of opportunistic behavior. The mere possibility of government abuse, however, should not deter implementation of an otherwise legitimate and effective program.

2. *Antitrust Challenges*

One of the most outspoken critics of TDR banks has been Norman Marcus. Marcus served as counsel to the city which pioneered the use of TDRs, but remained skeptical about their widespread use, especially when a government-run bank was part of the scheme.[231] In addition to being wary of possible strategic zoning, Marcus considered the potential violation of antitrust laws as a "major problem[ ]" with a city administered TDR bank.[232] If Marcus is correct and a successful antitrust challenge could be brought, it might result in the invalidation of a TDR bank as part of a zoning scheme.

Whether requiring all sellers to pool their TDRs, in an effort to promote urban planning goals, or forcing all sellers to trade through a middleman TDR bank, Marcus felt that an ordinance that concentrated all TDRs in one seller illegally reduced competition.[233] Marcus favored a system in which developers would compete for development rights and sellers would be free to sell to whomever they chose, within the confines of rational regulation.[234] In New York's singular experience with a TDR banking entity, the South Street Seaport develop-

See also infra Part III.A.4 (discussing wide latitude granted to governments that show legitimate public purpose for their action).

231 See Marcus, Transferable Development Rights, supra note 9, at 41-42 (summarizing major problems presented by TDR use: antitrust liability, lack of just compensation for "taking" property, spot zoning, negative effects of long distance transfers).

232 See Marcus, Air Rights in New York City, supra note 9, at 902 ("[I]f the city pays the owners just compensation for the development rights, stores them in the 'bank,' and sells them to developers, it may violate the antitrust laws."). Marcus believed that the option to sell TDRs in a private market was necessary to avoid a finding of "combination . . . or conspiracy, in restraint of trade," which is explicitly prohibited by the Sherman Act. Id. at 902-03 n.106; see also Sherman Act, 15 U.S.C. § 1 (1994).

233 See Marcus, Air Rights in New York City, supra note 9, at 902-03 n.106.

234 See id. at 902-03.

ment, the applicable zoning ordinance preserved an owner's right to sell the TDRs directly to third parties without use of the bank.[235] The preservation of this option, in Marcus's opinion, prevented the scheme from violating antitrust laws.[236]

States have been exempted from federal antitrust laws by the State Actor Doctrine set forth in *Parker v. Brown*.[237] In *Parker*, the Court held that state governments are sovereign within their territories, and that the purpose, subject matter, context, and legislative history of the Sherman Act gave "no hint that it was intended to restrain state action or official action directed by a state."[238] The Supreme Court concluded that trade "may appropriately be regulated [by states] in the interest of the safety, health and well-being of local communities"[239] and that the Sherman Act was not intended to prohibit acts of sovereign state governments.[240]

Local governments, unlike states, are not sovereign. Because of this fact, the Supreme Court wrestled with the extension of the State Actor Doctrine to local governments in *City of Lafayette v. Louisiana Power & Light Co.*,[241] *Community Communications Co. v. City of Boulder*,[242] and *Town of Hallie v. City of Eau Claire*.[243] While concluding that municipalities are not automatically entitled to immunity from federal antitrust laws under the State Actor Doctrine,[244] these cases established a test to determine when municipalities can be exempt from antitrust challenges.[245]

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235 See supra Part II.A.

236 See Marcus, Air Rights in New York City, supra note 9, at 898-99.

237 317 U.S. 341 (1943).

238 Id. at 351. The Court found instead that the Act's purpose was to "suppress combinations to restrain competition and attempts to monopolize by individuals and corporations . . . ." Id. at 351.

239 Id. at 362.

240 See id. at 352; see also id. at 359-60 (stating that state governments are sovereign in their actions "save only as they are subject to the prohibitions of the Constitution or as their action in some measure conflicts with powers delegated to the National Government, or with Congressional legislation enacted in the exercise of those powers").

241 435 U.S. 389 (1978).

242 455 U.S. 40 (1982).

243 471 U.S. 34 (1985).

244 See id. 38-39; *Lafayette*, 435 U.S. at 412 (stating that "municipalities . . . are not themselves sovereign," and therefore not beyond reach of antitrust laws).

245 The Court initially suggested in *Lafayette* that a municipality needed to show it was acting pursuant to a "clearly articulated and affirmatively expressed . . . state policy" that was "actively supervised" by the state. *Lafayette*, 435 U.S. at 410. In *Boulder*, the Court failed to find a clear articulation of state policy because Colorado's Home Rule Amendment conferred such general authority to municipalities to govern local affairs. Due to this absence of a clear articulation of state policy, the Court did not reach a decision as to whether a municipality must be actively supervised by a state. See *Boulder*, 455 U.S. at 51 n.14. In *Hallie*, the Court concluded that a broad authority to regulate, when it is "clear

The Supreme Court refined its test for extending the State Actor Doctrine to local governments in *City of Columbia v. Omni Outdoor Advertising, Inc.*[246] In *Omni*, the Supreme Court held that when a municipality's restriction of competition is an "authorized implementation of state policy," the municipality is entitled to *Parker* immunity.[247] The Supreme Court further held that state authority must be a "'clear articulation'" but need not be explicit; "[i]t is enough . . . if suppression of competition is the 'foreseeable result'" of the state-authorized action.[248] In *Omni*, the Court found that the state's grant of authority to zone inevitably involved some restraint on competition, such that the city was afforded *Parker* immunity from the Sherman Act.[249] Thus, if TDR banks can be seen as a mechanism of the zoning scheme authorized by a state zoning enabling act, or are explicitly authorized by a state as is the New Jersey Pinelands program, it is likely that they will be entitled to immunity from antitrust laws. However, the Supreme Court has held that this clear articulation is lacking in home rule states.[250] In *Community Communications Co. v. Boulder*,[251] the Court held that Boulder could not meet this requirement of the state action test because its home rule authority was so general.

An additional layer of protection for local governments is found in the Local Government Antitrust Act of 1984.[252] This Act provides immunity from "damages, interest on damages, costs, or attorney's fees" under Section 4, 4A, or 4C of the Clayton Act for "any local government, or official or employee thereof acting in an official capacity."[253] The Act similarly prohibits recovery in a claim against any person, based on "official action directed by a local government, or

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that anticompetitive effects logically would result," may suffice as a clearly expressed state policy. *Hallie*, 471 U.S. at 42. The Court also found that there is no requirement of active state supervision where the actor is a municipality. See id. at 46. Immunity from federal antitrust laws is also possible where state or municipal regulation is undertaken by a private party, but in that case both a clearly articulated state policy and active state supervision must be shown. See id. at 46 n.10.

246 499 U.S. 365 (1990).

247 *Omni*, 499 U.S. at 370.

248 Id. at 372-73 (quoting *Hallie*, 471 U.S. at 40, 42).

249 See id. at 371-74.

250 "Home rule" refers to the constitutional apportionment of power between state and local governments. Home rule states provide local cities and towns a measure of self government if they accept the terms of the state legislation, usually by adopting a "home rule charter." Given this authority to self-govern, local governments have the power to regulate without explicit authorization from the state. See Black's Law Dictionary 733-34 (6th ed. 1990).

251 455 U.S. 40 (1982).

252 15 U.S.C. §§ 34-36 (1994).

253 Id. § 35.

official or employee thereof acting in an official capacity."[254] In light of this Act and the Supreme Court's holding in *Omni*, it appears that local governments, like state governments, are well protected against claims of anticompetitive behavior.

None of the programs examined in this Note have been challenged on antitrust grounds. Each scheme preserved property owners' rights to sell their TDRs privately and utilized a TDR bank only as an alternative to private sale. In each case the bank was established to safeguard against an inability of TDR owners to obtain immediate compensation for the loss of their development rights due to the unavailability of a buyer.

The option to sell TDRs privately is especially important in Seattle, which does not enjoy the protection of the State Actor Doctrine due to the fact that Washington is a home rule state. In conferring general authority to govern Seattle's local affairs, Washington State has not clearly articulated a state policy to authorize anticompetitive conduct, thus failing the *Boulder* test. Given this vulnerability, Seattle, as well as other cities in home rule states, should be particularly aware of any anticompetitive behavior on its part, and should take special precautions to prevent antitrust challenges.

3. *Authority Challenges*

State governments, as sovereigns, possess the authority to exercise whatever powers are not explicitly reserved to the federal government.[255] They must show only that their actions comply with the United States Constitution; thus, any regulation of property must abide by the Fifth Amendment's mandate that no private property shall be taken for public use without just compensation.[256] Local governments, however, face an additional obstacle in that the authority to act must be granted to them by the state. Therefore, it must be determined that local government entities have the authority, properly delegated, to establish TDR programs and banks.

An ambiguous legal basis can give rise to delay or possible invalidation of TDR schemes through challenges in court. This uncertainty may impact voluntary landowner participation, which in many TDR

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[254] Id. § 36.

[255] See U.S. Const. amend. X ("The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people.").

[256] Regarding the Fifth Amendment, see supra note 8.

programs is central to the overall success of the preservation effort.[257] James T.B. Tripp and Daniel J. Dudek, Counsel and Senior Economist, respectively, for the Environmental Defense Fund, recommend that programs have "clear legal authority" to generate TDRs and implement and enforce a TDR program.[258] Even where express legal authority is not absolutely necessary to implement a TDR program and establish a bank,[259] Tripp and Dudek advocate obtaining it, if only to overcome agency and landowner hesitancy about participation.[260]

These concerns are all the more serious for TDR banks because they are, as yet, a new twist on traditional governmental regulation, even more so than TDRs. In order to allay landowners' concerns about the marketability of TDRs, TDR banks must be unquestionably legitimate. Given the wide latitude granted to localities to zone for the public welfare, it is likely that authority could be construed from a broad enabling statute but, for the reasons mentioned above, the TDR scheme itself will benefit from explicit authorization.

The four programs described in Part II present a range of situations that localities might face in the course of establishing their authority to create TDR programs and banks. New York presents a typical situation: The City's power to zone and regulate development within its municipal boundaries is granted by New York State's zoning enabling act.[261] Because South Street Seaport utilized a consortium of private banks rather than establishing a government operated bank, it has not yet been established whether the City has authority to create a TDR bank. Like many other states, New York's zoning enabling act does not explicitly mention TDRs or TDR banks,[262] but it does grant

257 See, e.g., Costonis, The Chicago Plan, supra note 9, at 588 (criticizing New York's landmark preservation program for relying on voluntary participation of landmark owners who "may balk, because they question the legality of the plan").

258 See Tripp & Dudek, supra note 9, at 375; see also supra note 92 (discussing details of Tripp & Dudek study).

259 A broad zoning enabling act, for example, might suffice to authorize a comprehensive land use scheme that includes the use of TDRs and a TDR bank.

260 Dennis J. McEleney, writing in the Illinois Bar Journal, expressed similar concerns about a lack of clear legal authority and recommended that enabling legislation specifically allow the enactment of a TDR program. See McEleney, supra note 9, at 640. In his opinion, municipalities without clear enabling legislation will be forced to construe this power "by implication or extrapolation of enabling statutes as a matter of public policy . . . ." Id.

261 Zoning is a state-held power exercised by local governments only at the will of the state, which usually grants local entities this power through a state zoning enabling act. See, e.g., N.Y. Gen. City Law § 20(24) (Consol. 1980) (granting New York cities power to regulate and limit height, bulk, and location of buildings so long as "such regulations may promote public health, safety and welfare").

262 This is changing as TDR use becomes more common. See Ariz. Rev. Stat. Ann. § 9-462.01 (A) (12) (West Supp. 1997) (specifically authorizing municipalities to establish procedures for development rights transfer); Ky. Rev. Stat. Ann. § 100.208 (Michie 1993) (au-

cities the power to "establish and maintain such institutions and instrumentalities" as they may deem "appropriate or necessary for the public interest or advantage."[263] It is likely that TDR banks created to facilitate legitimate TDR programs will be considered such instrumentalities.

Seattle's situation is different in that Washington, like many western states, practices home rule, so the City does not enjoy the validity of a state zoning enabling act's authorization.[264] Instead, Seattle has been granted broader authority to self-govern, which includes the power to exercise the police power normally reserved to the state. Seattle, then, finds itself acting as a sovereign only required to articulate a legitimate public purpose for its actions, but does not face a separate inquiry into its authority to act. As a result, Seattle probably has greater flexibility than most local governments to establish a TDR bank as a matter of public policy.[265] The ideal, but rare, situation is that of the New Jersey Pinelands, in which the government operated TDR bank is explicitly authorized by both state and federal legislatures.[266]

Of the four programs discussed in this Note, Maryland's Montgomery County is the only government that has faced a successful authority challenge, not to its TDR bank, but to its entire TDR program. In *West Montgomery County Citizens Association v. Maryland-National Capital Park & Planning Commission*[267] the Maryland Court of Appeals found an impermissible delegation of authority to the County Planning Board.[268] This challenge did not establish that the County lacked authority to enact a TDR scheme or bank, but rather

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thorizing any city, county, or urban-county government to implement TDR program); 32 Pa. Cons. Stat. Ann. § 5002 (West 1997) (defining TDRs).

263 N.Y. Gen. City Law § 20(16) (Consol. 1980).

264 See supra note 250 and accompanying text for an explanation of home rule.

265 McEleney observes that in Illinois, a home rule state, qualifying units of local government have constitutional authority to exercise any power and perform any function pertaining to government and affairs of unit. He interprets this to mean that local governments in home rule states have more power to implement TDR programs than local governments in states without home rule. See McEleney, supra note 9, at 640 & n.76.

266 See 16 U.S.C. § 471i (k)-(l) (1994); N.J. Stat. Ann. § 13:18A-31 (West 1997).

267 522 A.2d 1328 (Md. App. 1987).

268 The Maryland Court of Appeals held that zoning changes could not be made by amendment of a master plan, but had to be made by appropriate zoning procedures established by the state legislature in the state zoning enabling act. See id. at 1333-35. In addition, the court found that the Montgomery County Council impermissibly delegated zoning authority to the planning board. Because the legislature had not established precise standards for such zoning, the planning board was given an unlimited and invalid grant of authority. See id. at 1336-37.

that it had done so incorrectly.[269] This holding led the County to rezone pursuant to the state zoning enabling act, which remedied the authority problems and enabled the program to continue operating.[270]

4. Legitimate Public Purpose

Even when the appropriate government body has promulgated a regulation, the legislation may still face challenges to its legitimacy on the grounds that it serves an unacceptable purpose. The Fifth Amendment's language regarding "public use" has been interpreted to mean that government may take or regulate property only for such uses.[271] Thus, a legitimate public use, or purpose, is essential to the valid exercise of police power by the government. The public use requirement has been held to be "coterminous with the scope of a sovereign's police powers."[272] This is not a stringent requirement, however, as acceptable public purposes have expanded over the years to include much more than the original orthodox quartet of health, safety, morals, and general welfare.[273] Local governments may now rely on a broad range of aesthetic, cultural, and even fiscal justifications for their land use regulations.[274]

Much discretion is left to the regulating government, and courts grant great deference to legislatures in determining what constitutes a public purpose.[275] As the Court stated in *Berman v. Parker*,[276] "[W]hen the legislature has spoken, the public interest has been declared in terms well-nigh conclusive. In such cases the legislature, not

[269] See id. at 1329 (invalidating zoning decision made through planning process rather than through "zoning process mandated by State law").

[270] See Tripp & Dudek, supra note 9, at 382 n.36 (stating that "the County readily remedied the legal deficiencies").

[271] See supra note 8.

[272] Hawaii Hous. Auth. v. Midkiff, 467 U.S. 229, 240 (1984).

[273] See Village of Euclid v. Ambler Realty Co., 272 U.S. 365, 395 (1926) (holding zoning constitutional so long as it has "substantial relation to the public health, safety, morals, or general welfare").

[274] See, e.g., Village of Belle Terre v. Boraas, 416 U.S. 1 (1974) (upholding zoning ordinance which defined "family" and restricted inhabitants of household to two unrelated individuals); County Commr's. of Queen Anne's County v. Miles, 228 A.2d 450 (Md. 1967) (upholding five acre minimum lot size, a form of exclusionary fiscal zoning); State ex rel. Stoyanoff v. Berkeley, 458 S.W.2d 305 (Mo. 1970) (upholding aesthetic zoning regulation to maintain property values).

[275] See, e.g., *Midkiff*, 467 U.S. at 244 ("[I]f a legislature, state or federal, determines there are substantial reasons for an exercise of the taking power, courts must defer to its determination that the taking will serve a public use.").

[276] 348 U.S. 26 (1954).

the judiciary, is the main guardian of the public needs to be served by social legislation . . . ."[277]

As long as a public purpose is the primary motivation behind government action, it will serve a legitimizing role, regardless of other incidental effects the action may have. Responding to a challenge that the taking of private property through eminent domain and subsequent resale to a private developer was unconstitutional, the Supreme Court stated in *Berman* that once the public purpose is established, "the means of executing the project are for [the legislature and the legislature] alone to determine."[278]

In light of such Supreme Court holdings, it is unlikely that municipal ordinances that grant TDR banks the power to buy or condemn private development rights and resell them to private developers pose an obstacle to an otherwise acceptable exercise of the local government's police power. Costonis recognized two concerns related to this dynamic when he introduced the Chicago Plan.[279] The first was the criticism that his proposed TDR scheme served the interests of a distinct private group, namely the development rights purchasers.[280] The second was that government action taken to recoup costs of administering a public program delegitimized its public purpose.[281]

The strongest response to the first criticism is that the legitimate public purpose of preserving low-income housing, historic landmarks or districts, environmental areas, and farmland is the primary purpose of the government action. This defense is well supported by Supreme Court precedent.[282] As stated in *Poletown Neighborhood Council v.*

[277] Id. at 32. The scope of acceptable public purposes has expanded significantly to encompass a wide variety of motivating factors. The Supreme Court has found that the "concept of the public welfare is broad and inclusive." Id. at 33. The Court has construed the public use requirement so broadly that in *Midkiff*, 467 U.S. 229, it upheld an ordinance that took private property and sold it directly to other private parties in order to reduce concentrated land ownership. Finding this procedure "a comprehensive and rational approach to identifying and correcting market failure," the Court stated that "where the exercise of the eminent domain power is rationally related to a conceivable public purpose, the Court has never held [action] . . . to be proscribed by the Public Use Clause." Id. at 241-42. In fact, the Court held that "'[i]t is not essential that the entire community, nor even any considerable portion, . . . directly enjoy or participate in any improvement in order [for it] to constitute a public use.'" Id. at 244 (quoting Rindge Co. v. Los Angeles, 262 U.S. 700, 707 (1923) (second alteration in original)).

[278] *Berman*, 348 U.S. at 33.

[279] See Costonis, The Chicago Plan, supra note 9, at 603.

[280] See id.

[281] See id.

[282] See, e.g., *Midkiff*, 467 U.S. at 241-42; *Berman*, 348 U.S. at 35.

City of Detroit,[283] "condemnation for a public purpose cannot be forbidden whatever the incidental private gain."[284] Because legislators have broad discretion and receive such a high level of deference from the courts, it is extremely unlikely that any TDR banks will be successfully challenged on grounds that the legitimate public purpose for their existence is outweighed by the private benefit they create.

Like incidental private gain, incidental municipal gain also fails to overshadow a primary public purpose. The Supreme Court addressed a case in 1920 that presented a scenario quite similar to the one created by TDR banks. In *Green v. Frazier*,[285] a taxpayer suit against the state of North Dakota, plaintiffs alleged that the state was unconstitutionally taxing citizens to fund several public entities, including the Industrial Commission of North Dakota, the Bank of North Dakota, and the North Dakota Mill & Elevator Association. The plaintiffs charged that these bodies did not serve an exclusive or legitimate public purpose, as they were intended to generate profit to replace the general funds appropriated for their establishment.[286] They were also granted authority to exercise powers reserved for the government, such as eminent domain and regulation of prices, and they had authority to buy and sell on the market. These powers, and the mandate to generate funds, are very similar to those granted to many TDR banks today. In *Green*, the Court found that the "banking legislation" in question was justified by the public purpose of carrying out services needed by the industry and people of the state.[287] The Court further stated that even though the State was engaging in private industry, the entities created belonged to the State and did not have private gain as an objective.[288] The Court then held that "what was or was not a public use was a question concerning . . . local authority, legislative and judicial," and that those judgments would be "accepted by [the] court unless clearly unfounded."[289] Thus, it appears that as long as a legitimate public use, or purpose, is identified and served by a TDR bank, incidental private gain as well as incidentally generated municipal rev-

[283] 304 N.W.2d 455 (Mich. 1981) (holding alleviation of unemployment controlling public purpose which legitimized condemnation of residential neighborhood for sale to General Motors).

[284] Id. at 458; see also Gardner v. New Jersey Pinelands Comm'n, 593 A.2d 251, 263 (N.J. 1991) ("That a regulation provides an indirect benefit to others does not place it beyond the police power.").

[285] 253 U.S. 233 (1920).

[286] See id. at 235 (describing legislation in question as "having in mind the accumulation of a fund with which to replace in the general funds of the State the amount received").

[287] See id. at 240-43.

[288] See id. at 240-41.

[289] Id. at 242.

enue are well within a constitutionally acceptable assertion of the police power.

Each of the four programs examined in this Note was established to serve what have come to be accepted as valid public purposes. The preservation of historic landmarks has long been recognized as a legitimate public purpose.[290] Likewise, the preservation of low-income housing can be understood as promoting the general welfare. Thus, New York and Seattle are not threatened by challenges to the public purposes behind their use of TDRs or TDR banks. Montgomery County benefits from legislation that explicitly states a public purpose of farmland preservation.[291] New Jersey enjoys the benefit of both state and federal enabling statutes that recognize and declare that preservation regulations, including use of a TDR bank, are in furtherance of legitimate public purposes.[292]

B. *Financial Issues Facing TDR Banks*

In addition to legal issues, localities implementing TDR schemes that include TDR banks may face financial challenges. Some governments may find the costs incurred in establishing and operating a TDR bank prohibitive. Others may find that allowing TDRs to sit in a bank untaxed results in too great a loss of municipal tax revenues. Still others may become entangled in a combination of legal and financial problems as they attempt to place a value on the TDRs themselves. As the four programs highlighted in this Note demonstrate, these financial obstacles are surmountable, but should be anticipated and addressed at the outset.

1. *Municipal Revenue Problems*

As seen in Part III.A.4, challenges to the profit making function of a TDR bank do not preclude the use of such a bank. The other side of that coin, however, involves the costs a TDR bank imposes and may present more of a problem for some localities. Norman Marcus, viewing the situation from the government's perspective, has raised

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[290] See, e.g., Penn Cent. Transp. Co. v. New York City, 438 U.S. 104, 129 (1978) ("Because . . . [s]tates and cities may enact land-use restrictions or controls to enhance the quality of life by preserving the character and desirable aesthetic features of a city, . . . preserving structures and areas with special historic, architectural, or cultural significance is an entirely permissible governmental goal.").

[291] See, e.g., Functional Master Plan, supra note 180, at 27-31 (discussing farmland preservation as public purpose).

[292] See 16 U.S.C. § 471i(a)(2) (1994) (declaring "national interest in protecting and preserving [the] benefits" of Pinelands); N.J. Stat. Ann. § 13:18A-33(a) (West 1997) (creating Pinelands development credit bank as "instrumentality of the State exercising public and essential governmental functions").

some of these financial issues, including concerns about a TDR bank's impact on the tax base and the costs of purchasing TDRs.[293]

Whether a TDR bank is publicly or privately operated, a local government will lose tax revenues if it allows any TDR bank to act as a middleman in the transfer of development rights.[294] In direct transfer programs, either the seller or the purchaser could be responsible for paying taxes on the TDRs, regardless of whether they are used. With a government operated TDR bank serving as an intermediary in the transaction, however, the TDRs hang in limbo, are not assignable to any private party, and are not taxable. Therefore, the timing gap in TDR transfers will reduce the local tax base. Marcus questioned whether a private middleman would be willing to accept a tax assessment based on the unused development rights it holds and, if it did, whether such an assessment might threaten the profits and viability of the entity itself.[295] This is a valid and practical concern that should be addressed by any municipality that extensively utilizes a TDR bank.

Marcus's second practical concern specifically addresses government operated TDR banks and a city's ability to use scarce municipal resources to purchase and store development rights. He believes fiscal restraints have prevented many large cities from implementing TDR banks.[296] Marcus explains that these difficulties led New York to leave TDR trading to private markets.[297]

Not all TDR banks face financial barriers. In spite of Marcus's concerns, New York's South Street Seaport Consortium found the purchase and sale of TDRs to be profitable.[298] In another large city, Seattle's TDR bank is entirely self-sustaining. The City actually amended its original legislation one year after government appropriations for the bank ended and redirected its proceeds to a Low-Income Housing Fund.[299] New Jersey is unique in that it received funding from the federal government and so did not face significant revenue obstacles in establishing its Pinelands preservation program.[300] The Pinelands Development Project itself is anticipated to become a self-sufficient entity, however, as evidenced by the legislature's imposition of a time limit on its profitable operations.[301]

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[293] See Marcus, Air Rights in New York City, supra note 9, at 892, 903.

[294] See id. at 892.

[295] See id.

[296] See id. at 903.

[297] See id. (describing scarce municipal resources as one reason "New York City has preferred to leave TDR trading to the private market").

[298] See supra notes 112-13 and accompanying text.

[299] See Seattle, Wash., Ordinance 116366 § 6 (Sept. 28, 1992).

[300] See 16 U.S.C. §§ 471i(h), (k) (1994).

[301] See N.J. Stat. Ann. § 13:18A-47(c) (West 1997).

2. *Valuation*

A final issue presented by the use of TDR banks goes to the very heart of their purpose—valuation of the TDRs themselves.[302] It has been asserted that TDRs must be valued by the market, not a TDR bank.[303] This is due to the risk that the government will purchase TDRs for too little, the result of which would be a taking without just compensation.[304]

TDR banks are often created to set a minimum value for TDRs, thereby assuring that a fair price is given in exchange for restricted development rights. The very purpose of a TDR program, however, is to preserve public goods at a cost less than outright acquisition. These conflicting aims may tempt a government operated TDR bank to manipulate the market for TDRs to the detriment of TDR holders.[305] Just as a locality may not underzone property to devalue it, a locality should not be allowed to devalue a TDR by setting its price too low. Regardless of whether the bank then purchases the TDR or whether the private market then operates using this devalued price as a baseline, the TDR owner will be harmed.

Clearly this concern must be balanced against the opposing concern of ensuring a value for TDRs. Without a sure market, TDRs promise only speculative returns.[306] This is, in all probability, the strongest criticism of any TDR program.[307] The need, then, for TDR banks to set baseline prices and guarantee a landowner value may very well outweigh concerns about undervaluation. In any case, governments utilizing a TDR bank must consider the possibility of government abuse and provide some assurance that the TDR bank will not behave opportunistically. One way to ensure that TDR values are

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[302] See Kayden, supra note 9, at 579 (describing myriad questions raised in creating viable marketplace of property rights).

[303] See Stinson, supra note 13, at 344-45.

[304] See supra note 8.

[305] See Stinson, supra note 13, at 344-45; id. at 329 n.45 (noting that New Jersey Pinelands exchange (bank) has had significant effect on TDR prices; while purchasers have paid anywhere from $8,000 to $20,000 for each TDR, "'three-fourths of the sales have been at an [exchange-set] price of $10,000'" (quoting Richard J. Roddewig & Cheryl A. Inghram, Transferable Development Rights Programs: TDRs and the Real Estate Marketplace, 401 Plan Advisory Serv. Rep. 6, 6 (1987))).

[306] See, e.g., Fred F. French Investing Co. v. City of New York, 530 N.E.2d 381, 383 (N.Y. 1976) (holding grant of TDRs in exchange for rezoning land as public parks unconstitutional because "development rights with uncertain and contingent market value did not adequately preserve" property rights).

[307] See, e.g., Steven R. Levine, Environmental Interest Groups and Land Regulation: Avoiding the Clutches of Lucas v. South Carolina Coastal Council, 48 U. Miami L. Rev. 1179, 1210-12 (1994); Jennifer L. Bradshaw, Comment: The Slippery Slope of Modern Takings Jurisprudence in New Jersey, 7 Seton Hall Const. L.J. 433, 462-66 (1997) (criticizing speculative value of New Jersey's Pineland Development Credits).

set objectively might be to employ private appraisers and set TDR prices regionally, rather than on a case by case basis.

A different type of valuation concern was raised in Part III.A.1, which discussed the possibility that landowners may experience a decrease in property value as a result of TDR use. This could happen in two ways: First, landowners in preservation districts may lose value because of conservation easements, or their equivalent, that restrict development; and second, landowners in receiving districts may lose value because their development rights may be restricted in anticipation of future development right transfers. There might also be a reduction in property values due to speculative fears of overdensification without any offsetting preservation benefits within a given area.[308]

W. Patrick Beaton studied these effects on property values, using the New Jersey Pinelands Preservation Program as a case study.[309] Beaton selected three test areas—a preservation area, a development area, and a regional growth area, as identified by the Pinelands Comprehensive Plan—and compared their land values with those in control areas over a 20-year period.[310] Beaton found that the preservation area had a higher average annual price index than its control area by nearly 50% from 1972 to 1981, after announcement but before implementation of the preservation plan, and was over 40% higher between 1982 and 1986.[311] The development area experienced little price change net of its controls between 1966 and 1981, but following enforcement of the Pinelands Plan, price change grew at an average annual rate of 15% over its controls.[312]

Overall, market values of residential properties in both the preservation and development areas appear to have increased by more than 10%.[313] As could be expected, vacant properties in the preservation area decreased in value after growth controls were implemented. Real estate values in growth areas, however, after a temporary loss at the start of the growth control regime, rebounded.[314] Most impor-

[308] See supra note 33 and accompanying text (discussing long distance TDR programs).

[309] See W. Patrick Beaton, The Impact of Regional Land-Use Controls on Property Values: The Case of the New Jersey Pinelands, 67 Land Econ. 172, 172 (1991).

[310] See id. at 176-80.

[311] See id. at 188.

[312] See id. at 189. Short term residential resales in all three test areas began to inflate after announcement of environmental planning in 1972. See id. Overall, the anticipated suppression in the supply of buildable lots lead to an acceleration of price for residential and vacant land until enforcement of the growth control plan. Following this enforcement, the value of developed residential property in the growth controlled areas continued to outstrip those in nearby unrestricted areas. See id. at 191.

[313] See id.

[314] See id.

tantly, five full years after the implementation of the preservation program, there was no evidence of significant financial losses, but there were clear windfall gains for long term residential property owners in preservation areas. Price premiums of over 10% relative to their control areas commonly occurred after 1981.[315]

While this is only one study of one TDR program, it does provide evidence that the existence of TDRs, and a TDR bank, did not negatively impact land values for either transfer or receiving districts.[316] The results of this study may actually lend strength to the argument that TDR banks, by ensuring a stable market and sure value, counteract valuation and marketability problems that commonly afflict TDR programs. More empirical evidence is needed before this can be asserted with certainty, but it bodes well for TDR banks that the Pinelands, in which a TDR bank has broad powers and is central to the TDR scheme, is a successful and relatively untroubled program.

C. Recommendations to Localities Establishing TDR Banks

The ideal government operated TDR bank will anticipate and protect itself against each of the six issues outlined in Part III.A and B. In most cases this can be accomplished in the legislation implementing the bank itself. First, whatever potential incentives for strategic zoning that can be removed, should be. One step should be to ensure that revenue generated by the TDR bank is reinvested in the preservation program, not used to offset unrelated government costs. Another preventive measure would be to monitor closely any development restrictions imposed on receiving areas. Additionally, TDR owners should have the option of selling directly to private purchasers or to the TDR bank. Such a step would alleviate antitrust challenges and simultaneously prevent the government TDR bank from artificially depressing TDR prices. The bank should be clearly authorized, by the appropriate governmental body, to perform its necessary functions. These should include the power to buy, sell, hold, and acquire through eminent domain TDRs generated by the preservation program. Implementing legislation should include a clearly stated public purpose to ensure that any beneficial byproducts, whether to a private party or to the government, are recognized as incidental to a greater public good.

For the most part, the four programs examined in this Note follow the above recommendations. As these programs demonstrate,

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315 See id.

316 Nor does it appear that fears of strategic zoning have been borne out, at least inasmuch as landowners have not been hurt by depressed property values. See id.

however, strict adherence to these guidelines is not necessary, as they are simply that—guidelines. Each of the case studies is a unique example of a TDR program that uses a TDR bank to achieve its land use goals; together they illustrate the various ways in which successful programs may be structured.

Conclusion

Many criticisms have been leveled against TDR banks, some speculative, others more concrete.[317] After analysis of six primary concerns expressed about the use of TDR banks, it appears that each is surmountable by careful, comprehensive legislation. While there is always a possibility of government abuse, the existence of a TDR bank does not appear to alter government incentives to zone strategically or exacerbate negative consequences of a TDR program. To the contrary, a municipal TDR bank appears to have many more positive than negative effects on landowners, TDR purchasers, governments, and preservation efforts alike.

The limited scope of this Note did not allow presentation of the full range of creative TDR uses possible. Based on the survey of programs included, however, it appears that TDR banks are enabling cities, counties, and states to implement innovative and efficient land use programs by alleviating many of the basic deficiencies intrinsic to TDR programs.

If care is taken when implementing a TDR program that incorporates a bank and the recommendations made in Part III.C are followed, the benefits a TDR bank confers will outweigh any potential harms it might pose. Such an approach will enable local governments to continue enacting creative preservation programs which capitalize on the flexibility of TDRs, without the hazards of speculative valuation and market failure that have historically hobbled this valuable land use tool.

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317 See, e.g., Costonis, The Chicago Plan, supra note 9, at 602-31 (addressing legal challenges to Chicago Plan, including public purpose requirement, density zoning, and substantive due process); Kayden, supra note 9, at 571 (addressing charges of strategic or "incentive" zoning); Marcus, Air Rights in New York City, supra note 9, at 902-03 (raising antitrust and municipal revenue concerns).