

Paulo Sandroni



Paulo Sandroni graduated in economics from the University of São Paulo in 1964, and was a junior professor in economics in the Catholic University of São Paulo (PUC) until 1969, when he left Brazil during the military dictatorship. He taught at the University of Chile in Santiago until 1973, and later at the University of the Andes in Bogotá, Colombia, until 1979. After returning to São Paulo he again taught at PUC until 2006, and also joined the Business School of Getulio Vargas Foundation (FGV).

In 1988 after the victory of Brazil's Workers Party (PT) he joined the administration of São Paulo Mayor Luiza Erundina, where he directed agencies dealing with urban development and public transportation. During a short period he was also vice-minister of administration in the federal government.

In 1994 he left municipal government to continue his teaching and research on urban development in Brazilian and other Latin American cities, and to publish articles and books about economics, including a dictionary considered a primary reference in Brazil on economics. He began his affiliation with the Lincoln Institute in 1997. He is currently a private consultant on urban development and transportation issues, and continues to teach at the FGV Business School and in programs sponsored by the Lincoln Institute.

LAND LINES: *How did you become interested in urban policy issues given your background in macroeconomics?*

PAULO SANDRONI: In 1988 as an assistant to Luiz Inácio Lula da Silva, now Brazil's President and then a candidate in the elections of 1989, I helped develop programs to address Brazilian macroeconomic issues. After the victory of Luiza Erundina as mayor of São Paulo in 1988, I was invited to direct the city's program of *Operações Interligadas* (Linkage Operations). This involved negotiations and partnerships between the public and private sectors regarding additional building rights and the use of proceeds from the captured share of land value increment for the construction of social housing for poor families.

I also participated in the development of *Operações Urbanas* (OU or Urban Operations), a form of intervention to revitalize large areas of the city that also involves value capture. I was fascinated by the challenge to join the group whose mission was to govern Brazil's largest city with a strong social agenda, and I also continued to assist President Lula da Silva in macroeconomic matters until 1998.

LAND LINES: *Why do you consider urban development projects to be so challenging?*

PAULO SANDRONI: The primary reason is that large projects dealing with historical, cultural, social, and environmental aspects of the city must consider the economic and financial issues as part of the challenge, not the primary goal. For instance, OUs that seek to avoid gentrification and produce a more balanced social environment may have to use valuable land for social housing. These projects require special attention because the land cannot be sold using typical highest and best use criteria. There is an important distinction in Brazil between large urban projects (*Grandes Projetos Urbanos* or GPUs) that can be introduced with or without the value capture tools provided by OUs. By using those tools, however, it is easier to implement GPUs that increase both financial and social benefits for the private and public sectors.

LAND LINES: *Please describe the financial instrument behind this policy.*

PAULO SANDRONI: Since 2004 the source of funds to underwrite social housing and other infrastructure investments in OUs has been an ingenious new value capture instrument known as CEPACs (*Certificados de Potencial Adicional de Construção* or Certificates of Additional Construction Potential). One CEPAC may represent a different amount of square meters of additional construction rights depending on the OU where it was issued. For example, CEPACs ranged from a minimum of 0.8 to a maximum of 2.8 m² in Faria Lima OU and from 1.0 to 3.0 m² in Agua Espraiada OU, because land prices vary among different plots, even within the same OU.

The public administration that creates and owns the development rights can sell them to developers who want to build at higher density than was previously allowed on those plots. The CEPACs are sold by auction via the stock market, and prices can increase if interest among developers is high. The public sector does not need to price the asset, because the market does that. The income from the sale of CEPACs is under a strict law linked to a separate account used to fund infrastructure and social housing projects inside the OU, so there is no added pressure on the city's budget.

Many observers are suspicious of this instrument because they fear it is a form of land speculation in the financial market. I think this is a mistake for two reasons. First, aggressive speculators generally invest in bonds with high liquidity and sharp price increases in the short run; CEPACs have none of these characteristics. Second and more important, the government controls the market at this stage of the process. If prices increase due to speculation, the public sector can either sell these rights at a higher price, thus increasing its income proportionally, or it can sell a larger amount of the stock, thus provoking a fall in prices and neutralizing the speculators.

LAND LINES: *How have CEPACs actually worked in practice?*

PAULO SANDRONI: Both OUs mentioned earlier have used this instrument to raise funds

from developers. To date about 31 percent of the stock of square meters of CEPACs has been sold in the case of Agua Espraiada, and 32 percent in the case of Faria Lima. Agua Espraiada illustrates this bidding process and the influence of speculators. The city administration set up an auction in February 2008 for 186,740 CEPACs at an initial unit price of R\$ 460 (equivalent to US\$ 200). One party tried to buy them all, so the price rose to R\$ 1,110 (US\$ 480), an amazing increment of 141 percent.

Months later in October another auction offered 650,000 CEPACs for an initial price of R\$ 535 (US\$ 230), but only 379,650 were sold with no increment at all. From December 2004 to February 2009 the income from CEPACs in Faria Lima OU was R\$ 567 million (US\$ 244 million) and in Agua Espraiada OU it was R\$ 642 million (US\$ 276 million). If we compare this combined income of \$ 520 million over four years with \$ 1.25 billion collected in property taxes in 2008, we see that it represents more than 40 percent, or around 10 percent annually.

LAND LINES: *How can these examples be used to introduce support for alternative means to finance urban development?*

PAULO SANDRONI: The classic way to finance capital investment in infrastructure is through long-term borrowing and federal transfers; the property tax is generally used to maintain infrastructure and public services. But in Brazil, municipalities and states are subject to strict borrowing ceilings. The fact that CEPAC revenues are free of budget constraints adds significant financial value to the instrument.

In addition, as in the United States and elsewhere, raising taxes is very unpopular. In the last five elections in São Paulo at least three candidates have lost because voters considered them to be supporters of tax increases. Thus, to finance large urban interventions we have to assess the new value created, determine how to capture this value, and then create a win-win outcome. The CEPACs offer a viable alternative.

LAND LINES: *Are most large projects in Latin America prone to gentrification, and how can they be made more socially acceptable?*

PAULO SANDRONI: As long as GPUs focus on urban investments in infrastructure (construction of roads, bridges, malls, business centers, and the like), the price of land is likely to increase in certain affected areas, and thereby contribute to the expulsion of poor and even middle-class families. Nevertheless, these GPUs are public sector initiatives, so they can be designed to incorporate mechanisms to mitigate these exclusionary forces.

Brazilian legislation permits the establishment of ZEIS (*Zona Especial de Interesse Social* or Special Zone of Social Interest) in areas occupied by slums inside the perimeter of GPUs. In these designated areas, the developer is allowed to build only new housing for the poor, even if the land price is very high. Of course the economic and social opposition created by this mechanism is considerable among landowners and real estate developers, but is vigorously defended by local organizations and residents. São Paulo now has ZEIS within four GPU: Agua Branca, Faria Lima, Agua Espraiada, and Rio Verde-Jacu. The ZEIS in the Coliseu slum in Faria Lima and in the Jardim Edith slum in Agua Espraiada are interesting because they are located on the most expensive land within each of these projects (see Biderman, Sandroni, and Smolka 2006).

LAND LINES: *What are the downsides of these regulatory tools (CEPACs, ZEIS, OUs, etc.) that may leave loopholes for opportunistic behavior by well-positioned stakeholders?*

PAULO SANDRONI: Well, corruption and anti-social behavior may be found everywhere, and some conditions may facilitate it. But if you overload a system with regulations and norms, you may block initiatives to face new challenges and paralyze processes that can benefit the public interest. Reducing regulations and leaving more opportunities for negotiation is more risky, but you can mitigate the risk if you create norms on negotiation for which violation may result in very harsh punishment. At

the same time, there are certain issues that demand precise regulation, as in the case of ZEIS, because the poorest groups in the city require public sector intervention.

LAND LINES: *Can these kinds of development projects in São Paulo be replicated in other Latin American cities?*

PAULO SANDRONI: We have to be careful in transplanting or repeating experiences that were successful in one country to another one. It is important to know two things first: the conditions in the city when these OUs were created; and the kinds of problems the planners wanted these projects to solve.

For instance, an important condition in São Paulo is the separation of building rights from property rights, which opens the way to charge for changes in floor area ratios. In large areas of the city the floor area ratio, which relates to the right to build based on the zoning law, is now very low, ranging from one to two times the area of the plot. Where it is feasible for this floor area ratio to be increased three or four times without great pressure on the infrastructure, a charge is imposed on the owners or developers for the additional rights to build at a higher density.

In other cities where the floor area ratio is already high, there is less flexibility for charges on additional development rights, so other policies or tools may be required. The key lesson is that these OUs in São Paulo have shown that charging the owners or developers for the additional rights to build was both reasonable and fair. It is no longer socially, politically, or even economically admissible to grant these development rights for free. **L**

REFERENCE

Biderman, Ciro, Paulo Sandroni, and Martim O. Smolka. 2006. Large-scale urban interventions: The case of Faria Lima in São Paulo. *Land Lines* 18(2): 8–13.