

Lessons from the Latin American Experience with Value Capture

Martim Smolka
and Fernanda Furtado

Over the past five years, the Lincoln Institute has supported the study of value capture policies and instruments in many Latin American countries. Notwithstanding the diversity of approaches and the variety of specific cases, we have identified seven substantive lessons that can help to clarify some of the confusion and misunderstandings associated with the implementation of value capture principles. Each lesson summarized below presents one or two examples drawn from the book, *Recuperación de Plusvalías en América Latina: Alternativas para el Desarrollo Urbano*.

1. Value capture is not a new concept in Latin America.

The Latin American experience with value capture has long-standing historical precedents. Public debates on the use of value capture and related instruments have been held since the beginning of the twentieth century in several countries. In the 1920s, the debate was triggered by concrete events, such as the problem of paving streets in São Paulo, Brazil, and the lack of external financing for needed public works in Colombia. In other cases, political and ideological factors have motivated national discussions. Representatives of the *Partido Radical* in Chile made several attempts to introduce the idea, and in the 1930s President Aguirre Cerda proposed legislation to create a national tax on *plusvalías* (land value increments) based on the ideas of Henry George.

2. However, its application in the urban policy agenda is still limited.

Despite many reports of relevant experiences that integrate the principles of value capture, the issue is not well represented or even sufficiently acknowledged within the sphere of urban policy. In some instances, promising value capture initiatives have gained prominence in their own times, only to be forgotten later. An important example is the well-known *Lander Report* from Venezuela, which proposed in the

Value capture refers to the process by which all or a portion of increments in land value attributed to “community efforts” rather than land-owner actions are recovered by the public sector. These “unearned increments” may be captured indirectly through their conversion into public revenues as taxes, fees, exactions or other fiscal means, or directly through on-site improvements to benefit the community at large.

1960s that land and its increments in value should be the main source of financing for urban development projects. That report formed the basis for recommendations on urban development finance included in the proceedings of Habitat I (1976).

In other cases, interesting opportunities to use value capture as a tool for urban policy are being lost or ignored. Currently, some Latin American countries are not taking advantage of potential unearned land value increments generated by major inner-city revitalization projects. While there is general acceptance of the notion of capturing increases in land values, in reality little of that increased value derived from public action has actually been recovered and redistributed.

3. Legislation often exists but is not implemented.

As in many other countries in the region, the variety of value capture instruments available in Mexico, ranging from the *contribución por mejoras* (a special assessment or betterment levy aimed at recovering the costs of public works) to taxes on *plusvalías*, illustrates the discrepancy between what is legally possible and what is actually implemented. Contrary to what is often alleged, the general problem is not that the planners or local officials lack legal or practical access to these instruments but that the following conditions tend to prevail.

- The legislation and instruments are often conceived and designed (sometimes intentionally) in such confusing and contradictory ways that they virtually paralyze

any operational policy initiatives. For example, the Venezuelan national expropriation law of 1947 prescribes the taxation of 75 percent of land value increments related to public works, whereas the general municipal constitution (*Ley Orgánica de Régimen Municipal*) limits taxation to 5 percent of the total value of the affected property. In reality, even this limited charge is not collected.

- Even when the law makes value capture feasible, it may be difficult to interpret. For example, the debate between eminent jurists in the 1970s in Brazil with respect to the constitutionality of the legislation on *solo criado* (an instrument based on the separation of land and building rights) reflected a basic lack of understanding of legal precedents regarding value capture and its associated instruments.

- The possibilities of the law are not always widely known, even in their respective countries. This seems to be the case in Mexico, where the traditional property tax in the city of Mexicali, based on the combined value of land and buildings, was successfully replaced by a tax based exclusively on land value (Perlo 1999). Other cities in Mexico do not seem to be aware of or have not taken advantage of similar provisions in their state’s legislation.

4. Resistance is more ideological than logical.

Even when value capture legislation and instruments are understood (or in some cases because they are understood), they may not be implemented fully due to the proverbial “lack of political will.” This resistance may take the form of misleading interpretations, stereotyped rationalizations and even pure ideological “preaching.”

It is not hard to find public justification that the application of such instruments is neither timely nor appropriate, especially if the justification is based on misleading interpretations. Some such arguments are that impositions on land values are inflationary and disruptive of well-functioning markets, or that they incur unacceptable taxation of the same base twice. Such mis-

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conceptions seem to lie behind the reluctance of the Ministry of Housing and Urbanism of Chile to promote the review and resubmission to the Congress of some value capture provisions in the country's new legal framework on urbanism.

Objections based on stereotyped rationalizations may use the following arguments:

- the corresponding revenues are not significant or are not justified when compared with the administrative costs incurred;
- the public administrations would not be competent in terms of technical and human resources; or
- the application of value capture instruments would be antisocial and regressive, since the poor population, which has the greatest need for more urban infrastructure, has the least capacity to pay.

Contradicting these arguments, however, are the development of successful participatory improvement programs in poor areas of many cities (for instance in Chile, Brazil and Peru). These programs have been technically and economically efficient and usually have strong support from the low-income population affected.

Finally, some objections are of a purely ideological nature. The resistance to the implementation of *participación en plus-valías* in Colombia, for example, is based on the allegation that this device, although recognized as technically well-formulated, represents one more unwanted public “interference” on urban real estate business, such as a higher fiscal burden, limitations on property rights or more regulation (Barco de Botero and Smolka 2000). This position has been replaced recently by a broad consensus among politicians, business leaders and the general public that acceptance of this instrument is a better option than the imposition of additional property taxes.

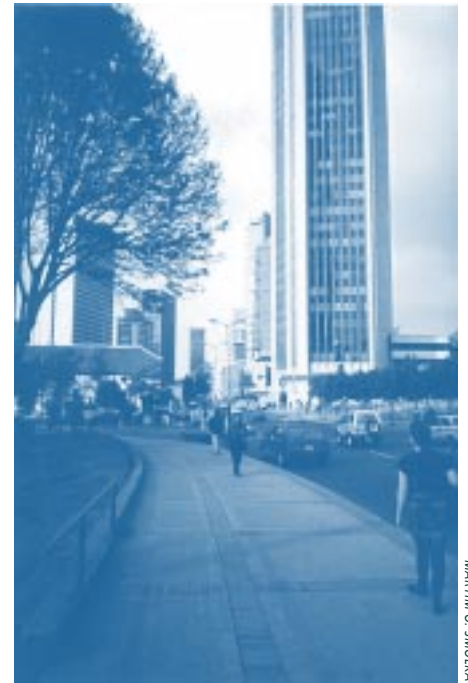
5. Value capture is gradually becoming more popular.

In spite of the obstacles and political resistance, recent Latin American experience with value capture shows a growing interest in the subject and in the conditions that would justify its utilization. Value capture is attracting the attention of municipal planners throughout the region, and it is beginning to be perceived as an important urban policy initiative. This growing popularity is related to several factors occurring in the region.

First, greater administrative and fiscal decentralization requires more autonomy in redefining and obtaining alternative sources of public funds to finance the urbanization process. The need for more local resources has been reinforced by the social demands and political pressures associated with current redemocratization processes and growing levels of popular participation. Formation of extra-budget funds to finance special social programs is linked to almost all new value capture initiatives and has been one of the most attractive reasons for implementing those policies.

Second, the redefinition of the functions of the state (including privatization), together with the decline of comprehensive planning, have set the stage for the development of more flexible public interventions and direct negotiations in land use regulation and public-private partnerships. The release of public areas to the private land market, as well as better coordination between real estate and public sector interests to promote new areas in the cities, are also significant. It is worth noting that even in Cuba one finds a vigorous program through which the Office of the Historian in Havana, operating as a kind of property holding company, refinances its state-owned operations with land value increments resulting from urban renovation projects in the form of rents charged to private development “partners” (Nuñez, Brown and Smolka 2000).

Other favorable factors include the conditions imposed by the agendas of multilateral agencies, which clearly promote the universalization of user charges and the recovery of the costs of public investments. The growing popularity of new value capture instruments can also be attrib-



MARTIN O. SMOLKA

Downtown Bogotá, Colombia

uted to some frustration with the poor results obtained from the application of taxes and other traditional charges related to urban land in past decades, in terms of both revenues and urban policy objectives.

6. Pragmatism overrides ethical or theoretical justifications.

A corollary to the preceding point is that the growing popularity of value capture seems to be inspired more by eminently pragmatic reasons than by ethical criteria, notions of equality, or theoretical and political justifications. Some reforms may even have been introduced without full political awareness of the process, or of its theoretical importance, as previously illustrated in the Mexicali case. The historical evidence shows that most value capture initiatives have responded above all to the need to face fiscal crises and other local problems in the financing of urban development. This is the case even in Argentina, where the need for revenues prevailed over established principles opposed to new taxes when a temporary five-percent increase in the property tax was used as one of the initiatives to finance investments in the new Buenos Aires subway system.

Nevertheless, one should not assume from the above examples that accumulation of experience is not important for the refinement of instruments and the evolution of value capture policies. A case in point is the Colombian experience with the *contribución de valorización* since the 1920s and the many attempts to overcome some of its limitations, especially in the past 40 years. The recently enacted *participación en plusvalías* is a more technically developed and politically acceptable version of an instrument targeted to capture the sometimes huge land value increments associated with administrative decisions concerning zoning, density levels and other urbanistic norms and regulations.

7. Value capture is not necessarily progressive or redistributive.

It must be noted that the reference to *plusvalías* is in no way a monopoly of the political left. Both Argentina's and Chile's recent experiences show clearly the disposition toward the subject in neo-liberal contexts. In addition, the *operações interligadas* (linkage operations) developed in São Paulo, and effectively applied by administrations of opposing political and ideological tendencies, put forward a convincing argument about the impossibility of labeling these instruments in advance.

Progressive local governments, on the other hand, are sometimes reluctant to apply these instruments, and may even reject the notion altogether, for three reasons. First, they may believe that such contributions would be simply a mechanism to impose additional fiscal charges with no redistributive impact whatsoever. Second, even when the resulting revenues are earmarked for the low-income population, they may be insufficient to reduce the absolute differences between rich and poor in the access to the serviced land (Furtado 2000). And third is the intergenerational argument that such charges are being imposed on newer, generally poor, residents who need services, whereas earlier generations were not charged for infrastructure services or amenities.

Thus, the progressive nature of such policies is not resolved by "taxing" land value increments or by focusing on high-income taxpayers. The "Robin Hood" image of such policies fades once it becomes clear that the part of the value actually captured in this way tends to be only a fraction, and often a small one, of what the owner actually receives in benefits. This point seems to have been well understood by many lower-income populations, like those in Lima where a successful program featuring some 30 projects used the *contribución de mejoras* to finance public works in the early 1990s.

This example and other strong evidence support the need to revisit the conventional wisdom regarding the tension between the principles of benefit and capacity of payment. In practice, the strategy of attracting some public intervention to one's neighborhood (even if it means paying for its costs) is more advantageous than the alternative of being neglected. This point should, nevertheless, be taken with caution, in light of certain experiences where the *contribución de mejoras* has been applied in low-income areas with purposes other than benefiting the occupants—for example, to justify the eviction or force the departure of those who cannot pay for the improvements (Everett 1999).

Final Considerations

In spite of the difficulties in interpretation and resistance to implementation outlined above, value capture policies are undeniably arousing new interest and growing acceptance. Efforts to utilize value capture have grown in both number and creativity, and its virtues beyond being an alternative source of public financing are becoming better understood. Public administrations are realizing the "market value" of their prerogative to control land use rights, as well as to define the location and timing of public works. They also see that the transparent negotiation of land use and density ratios reduces the margin of transactions that used to be carried out "under the table." As the link between public intervention and land value increment is becoming more visible, attitudes are changing to be more conducive to building a fiscal culture that will strengthen property taxes and local revenues in general.

However, there is still much to be done in two spheres: researching the complex nature of value capture policies and promoting greater understanding among public officials with regard to how it can be used to benefit their communities. More knowledge is required on certain Latin American idiosyncrasies, such as when significant land value increments are generated under alternative land tenure regimes that are outside the protection of the state, and in cases where the land represents an important mechanism of capitalization for the poor.

Beyond the traditional, structural constraints of patrimonialism, corruption, hidden interests, ideological insensitivity and the like, a considerable part of the "unexplained variance" in different experiences with value capture in Latin America can be attributed to lack of information. Toward that end of improving understanding of the principles and implementation of value capture, there remain many opportunities to document and analyze current experiences with alternative land valuation and taxation instruments. □

Martim Smolka is a senior fellow and the director of the Lincoln Institute's Latin American Program, and **Fernanda Furtado** is a fellow of the Institute and a professor in the Postgraduate Program in Urbanism at the Federal University of Rio de Janeiro. Contact msmolka@lincolninst.edu or furtadof@gbl.com.br.

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NOTE

These *Land Lines* articles and many other papers on value capture in Latin America are available on the Lincoln Institute website, and most are available in English and in Spanish or Portuguese. (www.lincolninst.edu)