



The potentials of Land-based financing instruments

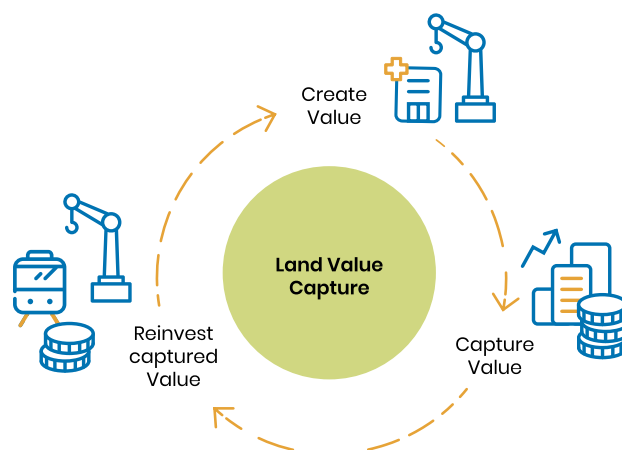
General concept & Insights from two studies

The concept of Land-based financing

Cities have an annual demand for infrastructure investments of around 4.5 to 5.4 billion USD globally. However, around 1 billion USD are lacking to meet this demand. The concept of Land-based financing (LBF) with a variety of different tools is one way to contribute to closing of this investment gap. The concept of Land-based financing is based on the idea that the value of land increases as a result of public action, such as investments in infrastructure, land use changes or other urban development projects. The construction of a new transportation network or the development of new public amenities for instance can increase the value of nearby land. The idea of Land-Based financing is, that local governments would be able to benefit from this increase in land value to generate revenue for the public good instead of leaving the whole benefit of public investments to private landowners. LBF is based on the principle that public action and investment generate a public benefit. Through certain measures, these benefits can be partially recovered or „captured“ by the public sector for reinvestment, and thus not only benefit private owners. LBF instruments, therefore, aim to increase the share of profits captured by the public sector (at the expense of the share held by private investors). There are different forms of Land-based financing instruments, ranging from those meant to support initial investments and ongoing maintenance of

infrastructure and urban development projects in a specific area, such as betterment levy, to those that increase the local revenue sources in general, such as for instance property taxes or development fees. Ideally, Land-based financing instruments should contribute to a virtuous cycle of public investment, public value capture and public reinvestment of land values captured, supposed to serve society in the long term (Image 1).

Image 1: The virtuous cycle of public investment



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The application of Land-based financing instruments for urban management can play an important role in shaping the cities of tomorrow. Strengthening the financial capacity of cities, Land-based financing paves the way for potential new investments in urban areas. Land-based financing is also a tool to achieve sustainable and integrated urban development. It can thus contribute to achieving the objectives for sustainable urban development set in different international and national agendas, such as the Agenda 2030 on Sustainable Development of the United Nations, the BMZ core area strategy “Responsibility for Our Planet – Climate and Energy” or the BMZ position paper on Sustainable Urban Development.

To promote the many opportunities that Land-based financing holds, the GIZ Sector Project “Cities” has elaborated and published two studies in 2021 and 2023. These analyze the potential of Land-Based financing, its implementation in different contexts and key factors for the success of the various instruments. The first study “Land-value capture for Urban Development – Knowledge Report”, published in June 2021, draws lessons from the analysis of frameworks and implementation experiences of Land-based financing instruments in 10 countries: Ecuador, Egypt, Ethiopia, Ghana, Indonesia, Morocco, Namibia, Peru, Tunisia, Ukraine. It highlights three levels of LBF:

- **Macro-level instruments** focus on controlling the land market of an urban area, ensuring that land for public use is or becomes available (land banking), or realigning land (land readjustment or land reallocation) for the planning of infrastructure. They include land nationalization, land banking, long-term public leasehold systems, and land readjustment. Hence, the purpose of capturing increased land value is only a secondary mean.

- **Direct value capture instruments**, that are designed to legally oblige landowners to contribute a share of their land value increments, such as taxes in case of market-caused increments, or betterment levies after governmental decisions or acts of planning.
- **Indirect value capture instruments**, that are more locally established and often negotiated with the developers. They are not constituted in national law, which makes them useful to quickly react to market changes. They include exactions, inclusionary zoning, impact fees, and transfers of development rights.

The analysis of the reviewed cases where land-based financing instruments have been implemented also shows some of the main bottlenecks and risk factors for their successful application. These usually are:

- The technical and human resource capacities to handle, evaluate and update the land valuation systems,
- The need for a clear legal framework to set boundaries, which fees can be raised, that are in line with the LVC instruments (national urban policies, municipal regulations),
- Clear mandates and transparent ways of implementing instruments and reinvesting the collected revenues in infrastructure measures.

The second study “Land-based financing for Urban Development – Implementation Examples”, published in February 2023, provides a compilation of implementation experiences of 16 different instruments from the different categories (macro-level, direct value capture, indirect value capture) from 15 different cities around the globe.

Macro-level instruments

The experience of Addis Ababa with the use of Land-based financing instruments for the development of an urban renewal project

In the Ethiopian city of Addis Ababa, urban authorities used macro-level instruments to largely fund the development of the Lideta urban renewal project. The project was implemented with the objectives of an inclusive revitalization and road network improvements. It was funded through land leasing of governmentally owned land to private investors, property taxes as well as the sale of commercial buildings and housing. Land leasing was established to transfer land-use rights for a fee that could then be used by the government to reinvest in infrastructure and affordable housing. The revenues gained through land leasing covered the main proportion of the redevelopment costs for the Lideta project. Property taxes enabled the city's government to collect taxes through increased property values due to public infrastructure investments. The sale of publicly owned housing and commercial buildings generated additional revenues to reinvest in future urban developments and affordable housing units. The initial investment of the government for the implementation of the project had been 42.3 million USD supplied by the city budget. Through the application of the various Land-based financing instruments, the government was able to collect 17.4 million USD as revenue so far. The potential revenues are estimated to be around 41.6 million USD, almost entirely covering the initial expenses.

Direct value capture

The experience of the city of Bogota (Colombia) with the implementation of a betterment levy

A betterment levy is implemented as a direct value capture instrument. Its basic idea is the contribution of private landowners for the funding of basic infrastructure that directly benefits them. It can be charged before, during or after the completion of the project. The basis for the payment of the contribution is the Factors Benefit Model, which is used to estimate the land value increase (or valorisation) through the distance of a specific land plot to a new infrastructure project. It has four categories that assign a valorisation percentage according to distance (Table 1).

Table 1: The Factors Benefit Model

Benefit degree	Distance in meters	Valorisation %
1 st degree: maximum	1,000	15 to 25
2 nd degree: medium	2,000	10 to 15
3 rd degree: minor	3,000	5 to 10
4 th degree: minimal	5,000	5 or less

The city of Bogota has been able to collect revenues ranging from 100 million up to 1 billion USD in different projects since 1993. A key aspect for the success of the betterment levy is finding the right balance between the taxpayers' payment capacity and a just levy contribution. Hence, the payment cannot be higher than the double amount of the property tax fee and it may be divided into smaller amounts over a two- year period. Furthermore, it is crucial to ensure a clear cost-benefit relation of the payment and the Betterment Levy, the involvement of citizens in a transparent process on how the amount of the contribution is defined, as well as the support of local politicians in order to successfully implement Betterment Levy.

Indirect value capture

The experience of Surabaya (Indonesia) with the implementation of indirect value capture instruments

In Indonesia, the city of Surabaya established several indirect value capture instruments to respond to the strong increases in property prices and control the planning and sustainable development of new high-rise developments. Thus, the city's government additional negotiable developer obligations to increase public revenues when high-rise buildings are being developed in addition to the already existing non-negotiable developer obligations. Non-negotiable developer obligations included fees during the pre-construction (fees to obtain development and pre-construction permits), as well as during and after the construction process (i.e. advertising tax, land and building tax, waste retribution) (Table 2).

According to national law and a municipal regulation, the additional negotiable developer obligations for the construction of high-rise buildings can be required by the municipality as a condition for granting a development permit for a site, especially, when a specific infrastructure or utility required according to the masterplan is still not available. The municipal regulation specifies the contribution as a proportion of the land that will be used for public infrastructure, its type and size depend on the proposed development. The specific public infrastructure that needs to be provided by the developer can still be subject to negotiation.

As a result of the introduction of the negotiable developer obligations, the municipality has been able to fund the development of several infrastructure projects to improve nearby areas. However, this practice has also led to discussions and complaints by private developers. As a result, the municipality must now ensure, that developers can share the benefit of their own contributions by using the collected fees only for on-site facilities that add to the quality of the location where a high-rise building has been developed.

Table 2: The Factors Benefit Model

NO	Stage of Development	Types of revenue source	Government regulation
1.	Pre-Construction	SKRK retribution 1MB retribution	Municipal Regulation no.5/2012. Municipal Regulation no.12/2012.
2.	Construction	Advertising tax Land and building tax Hotel tax Restaurant tax	Mayoral Regulation no.14/2009. Municipal Regulation no.10/2010. Municipal Regulation no.4/2011. Municipal Regulation no.4/2011.
3.	Operational	Street lighting tax Acquisition tax (BPHTB) Advertising tax Waste retribution	Municipal Regulation no.4/2011. Law no.20/2000 Mayoral Regulation no.14/2009. Municipal Regulation no.10/2012.

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