SPECIAL SECTION:

DRIVERS OF OUTWARD MIGRATION AND BARRIERS TO REDEVELOPMENT IN NORTHEAST OHIO

SUMMARY

The principal theme emerging from the Vibrant NEO 2040 visioning process is the need to reinvest in Northeast Ohio's established communities. Since the 1960s, these places have experienced significant population loss and disinvestment, while progressively larger and lower-density rings of suburban development have pushed the footprint of urbanization outward. The resulting conditions in the traditional cores—deteriorated physical fabric, stressed budgets, and socioeconomic dislocation—are impeding the region's ability to compete nationally and internationally for businesses and workers, who are increasingly seeking out vibrant urban places in which to settle and work.

In recent years, an emerging community of developers has taken on substantial risks to invest in the region's legacy communities. From Cleveland to Akron, Youngstown to Kent, Lorain to Canton, these developers are creating value in place, and attracting exactly the kinds of businesses and economic activity that the region must continue to cultivate to succeed in the 21st century. Yet the scale and pace of this investment has still not reached a critical mass regionally. As a corollary to the research and scenario planning work of Vibrant NEO 2040, the Project Team has pursued an investigation into the barriers to achieving more substantial urban redevelopment and infill development. Interviews were conducted with a range of actors in the development ecosystem, including developers, brokers, financers, lawyers, community organizers, and public officials.

These interviews, coupled with research into secondary sources and literature, revealed nine significant barriers to urban redevelopment in Northeast Ohio:

- High costs relative to market prices
- Complicated financing structures
- Coverage and direction of publicly-funded incentives
- Uncertainty in interactions with regulations and regulatory entities
- Perceptions of municipal service quality
- Unaccounted subsidies in public infrastructure
- Misallocation of authority to levy impact fees on development
- Asymmetries in taxing powers and practices between political subdivision types
- Differences in sophistication and rigor of zoning and development review processes

This section elaborates upon the above barriers and analyzes their causes and consequences for the region's development patterns. It concludes with a discussion of two organizational forms—publicly-formed (Joint Economic Development Districts and Cooperative Economic Development Agreements) and privately-formed (Special Improvement Districts and Community Development Corporations)—that crystallize the ways in which law and fiscal politics affect development outcomes.

ENDOGENOUS VS EXOGENOUS BARRIERS

In the course of secondary research and interviews with developers, it became clear that some barriers have an internal cause or origin and are endogenous in nature and others are the result of external factors and are exogenous in nature. Endogenous barriers arise from the particularities of working in the urban environment on redevelopment projects, whereas exogenous barriers arise from asymmetries between development environments. Both forms of barriers have different implications for development behavior. The exogenous barriers tend to distort development behavior through perverse incentives for new development on greenfield land, preventing more developers from entering the redevelopment market. The endogenous barriers tend to be more process-oriented, influencing developers' willingness to scale operations after an initial project experience as well as the external perceptions of developers considering commitment to a project.

ENDOGENOUS BARRIERS

1. High costs relative to market prices

Every interviewee cited cost as a leading barrier to redevelopment and urban infill. Redevelopment project costs are generally 2 to 3 times greater than in greenfield contexts for commercial office products: most projects require rents of $35-$40 per square foot in order to produce positive cash flow, whereas the upper end of the regional market for commercial office projects is closer to $20-$25 per square foot.

The higher costs of redevelopment are driven by several realities that are distinct from other development locations such as suburban greenfields. Principal among them is the need for complex parcel assembly, a process which can take years and involve considerable expense, as well as environmental remediation. Many established communities in Northeast Ohio bear the toxic legacies of their industrial past, present in both land and buildings, which require often extensive and thus costly cleanup activities. Also a considerable driver of higher costs is the expense associated with bringing buildings up to code, especially if the project involves adaptive reuse. The construction materials used for the reuse of older buildings may be more expensive per unit cost than new construction, especially if historic preservation ordinances are in effect (which several communities in Northeast Ohio have). Building structured parking to accommodate higher densities also drives costs up and requires high parking charges that few consumers in Northeast Ohio are willing to pay.

While potentially adding value to a development and the community at large in the long run, another factor associated with higher costs are the special improvements required in development agreements with municipalities. These often appear as a result of a district-level plan, master plan, or overlay ordinance, and sometimes at the behest of surrounding property owners. Such special improvements, whether streetscape improvements or site-specific enhancements, usually add both hard capital costs (through constructions or direct payments to a city or designee) and soft costs (attorney and architecture/engineering consulting fees) to the project and are more difficult to project and account for in a pro forma than other cost drivers.

2. Complicated Financing Structures

The costs and risks associated with redevelopment and infill projects often make it difficult to secure financing from traditional sources of debt capital, even for the most experienced developers. This is especially true in the aftermath of the financial crisis of 2008, with many financing deals for projects entering development pipelines prior to the crisis, falling apart and forcing developers to seek capital elsewhere or walk away from projects.

The financial crisis notwithstanding, urban developers need many layers of capital to finance project costs and make products economically viable, much of which come from public sources such as tax credits and tax increment financing. Federal New Market Tax Credits (NMTC) and federal and state historic tax credits provide highly valuable financial subsidies to redevelopment and infill projects. Discretionary grants from federal and state programs like EPA Brownfields Funds can also be important sources of financing, though these are less reliable.

Layered financing is cumbersome to track and manage, especially when public and private capital are in the equation. Public funding typically requires detailed reporting and documentation of work and decisions. Many developers have neither the experience nor the desire to undertake publically underwritten development. The Flats East Bank project in downtown Cleveland, for example, required 34 layers of private and public capital, and took eight years to assemble. Few developers in markets like Northeast Ohio's will have the time, financial resources and persistence to devote to a single project like the Flats East Bank.

3. Coverage and Direction of Publicly-Funded Incentives

Most public subsidies and tax credits are statutorily directed to meet a politically defined need, such as rehabilitating historic buildings or bringing development into low-income neighborhoods. This is not an issue when a development is among the first in an economically depressed area, but it quickly becomes an issue as activity intensifies. Sometimes an area loses its eligibility for low-income tax credits as higher-income residents move in. In other cases, the supply of buildings eligible for historic tax credits runs out. In many cases, several developers noted, the crucial gap financing offered by public subsidies disappears before the market justifies private financing, squelching development prospects. This was characterized by one developer as "incentives that punish success."

As a corollary, several developers indicated concern with how public subsidies were directing development activities on urban land. These centered in particular on the historic tax credits, which sometimes induce rehabilitations of "historic" buildings on plots that would otherwise be better suited for higher floor-to-area ratios or more intensive uses than what they end up hosting. Such effects distort the urban land market and can frustrate other policy goals of a municipality. Even more concerning to one interviewee was the prospect of a future collapse in market activity once the exhaustion point was reached for sensible historic retrofits. This interviewee, a major player in development of housing in the Midtown area of Cleveland, noted the need for thought and action on creating new incentives that would encourage redevelopment of vacant land as opposed to just historic buildings.

4. Uncertainty in Interactions with Regulations and Regulatory Entities

An interesting pattern that emerged from interviews was the sharp divergence in perspectives on navigating local regulatory processes and managing relationships with public officials. While comfort and ease with regulatory process tends to grow with completion of successive projects, a poor experience for a newcomer to a particular jurisdiction will undoubtedly discourage them from pursuing future development opportunities.

Though frustrations with more complex zoning, permitting, and inspections are typical and even to be expected, the most important driver of uncertainty, as characterized by interviewees, is the prospect of NIMBYism, or the tendency of some neighbors to object to projects in their community, declaring "Not in my backyard." NIMBYs have a curious effect on the process, as they can force the municipality to assume a potentially more adversarial regulatory posture vis-à-vis a proposed development. One experienced homebuilder likened it to siblings vying for the attention of a parent who clearly favors one over the other. Once neighbors decide to oppose a project, on whatever grounds, the process becomes politicized and schedules can become delayed by weeks and months.

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5. Perceptions of Service Quality within a Particular Municipality.

While not directly cited by most interviewees, one developer concluded his remarks with a thought that the condition of poorly-performing inner-city school systems was the number one barrier to scaling redevelopment in the region. Though it may not be appropriate to classify education alongside other municipal services (generally, school districts are their own jurisdiction) such as trash collection, police and fire, 911 services, etc., perceptions of service quality are influential in both developers' decision to enter a market as well as their read of potential customer's interest in purchasing a product in that market.

EXOGENOUS BARRIERS

1. Unaccounted Subsidies in Public Infrastructure.

Significant subsidies are granted to develop infrastructure that facilitates the spreading outward of population and, in some cases, the poaching of jobs and employment from one area of Northeast Ohio to another. This is driven, in part, by planning processes that emphasize traditional capacity expansion in an effort to mitigate traffic congestion, thus channeling federal transportation dollars into road widening projects, which sets the stage for local jurisdictions to permit housing and commercial growth on greenfields. It also occurs through programs that, under the aegis of rural development, favor counties and townships over cities, such as a program that subsidizes construction of wastewater treatment and conveyance infrastructure that can spur greenfield development. The existence of such programs contrasts sharply with the lack of similar programs for established cities, such as a fund to help cities meet U.S. EPA MS-4 obligations to separate sanitary and storm sewers.

2. Misallocation of Authority to Levy Impact Fees on Development.

Among the most interesting and salient of the exogenous barriers to redevelopment is the question of impact fees. Impact fees are one-time charges assessed to new developments that offset the additional costs of providing public services. Ohio is one of 22 states that, as of 2013, does not have enabling legislation authorizing political subdivisions to levy impact fees. In the vacuum of a legislative definition of impact fees and the acceptable methodology for their calculation, courts have had to step in with their interpretation. A case brought before the Ohio Supreme Court in 2000, Homebuilder's Association of Dayton and the Miami Valley, et. al. v. City of Beavercreek, resulted in a divided court ruling that local jurisdictions did have the authority under their constitutionally defined police power to levy impact fees that passed a rational nexus test. In the wake of the ruling, several municipalities and townships (though none in Northeast Ohio) adopted impact fee ordinances.

The Ohio Supreme Court partially reversed its earlier decision on impact fees in Drees Company, et. al. v. Hamilton Township, in 2012. In Hamilton, the Court ruled that townships, which have only limited home rule powers, could not levy impact fees, as they are an unconstitutional tax with respect to the powers of the state. Though incorporated municipalities, which have home rule powers, are still permitted to levy impact fees under their police powers, impact fees do the most good in terms of allowing for planned, fiscally sound growth where growth actually occurs. In Northeast Ohio, a considerable and increasing percentage of new housing growth occurs in townships. The decision highlights the vacuum of state law governing impact fees. The practical consequence of the absence of a region-wide approach to levying impact fees for new development is a virtual subsidy to greenfield development, further sapping the market for urban infill and redevelopment.

3. Asymmetries in Taxing Powers and Practices between Political Subdivision Types

Closely related to the unequal allocation of the ability to levy impact fees is an asymmetry in how state law distinguishes the taxing powers and practices of municipalities, which are incorporated, and townships, which are not. Though Ohio is a home rule state that reserves substantial powers to local jurisdictions, full home rule powers are apportioned only to municipalities, which enjoy a more comprehensive control over questions of taxation.

There are a several critical distinctions between municipalities and townships on taxation. First, townships tend to have a much lower property tax mill than municipalities, owing to the less developed extent of services they provide. This makes township land attractive for commercial developers, provided sufficient infrastructure already exists or can be provided. Households looking to minimize tax liabilities in exchange for the prospect of providing more services for themselves are also incentivized to locate on township land.

The most salient distinction between the two entities centers on income tax. Municipalities are empowered to collect income tax from residents under home rule, whereas townships are not. The presence or absence of income tax is often a consideration both for employers and households. One interviewee spoke about the powerful effects of income taxation on the decisions of entrepreneurs faced with the prospect of double taxation if both their home and business is located in a city with a municipal income tax. The interviewee hypothesized that this could be a deterrent for new companies looking to establish or expand operations in Northeast Ohio's cities.

4. Differences in Sophistication and Rigor of Zoning and Development Review Processes

Significant differences exist between local jurisdictions with respect to their development planning and review capabilities. Some of these differences can be attributed to state statute: Municipalities in Ohio are required to have and maintain a master plan and accompanying zoning, whereas townships are enabled but not required to maintain zoning. Most Wayne County townships as well as townships found in Ashtabula, Trumbull, Mahoning, Geauga, Portage and Stark counties have choose not to adopt zoning. Some of the differences between municipalities and townships can be attributed to differences in administrative capacity and available resources: Whereas municipalities have planning and zoning departments often with full-time staff or contract consultants, townships rarely have comparable resources and, if they have adopted zoning codes, must rely on the services of a part-time zoning inspector, a volunteer zoning commission and, in some counties, the staff of their county planning department to administer them. Without the statutory obligation or the administrative capacity to engage in land use planning or update their zoning codes and maps, townships may find themselves unable to keep pace with shifts in the region's real estate market.

While many developers find the low-oversight environment of townships to be appealing, others have found it frustrating, particularly when seeking to build more compact forms of housing or mixed-use commercial development. One interviewee, an experienced builder in both urban and rural communities in Northeast Ohio related his frustration in trying to introduce small-lot traditional neighborhood development in communities which lack both the code language to permit this style of development and the administrative capacity to either interpret or amend their code to meet contemporary market demand. Another developer experienced in both urban redevelopment and suburban greenfield building described the relationship between the regulatory posture of a municipality and its development maturity as an artificial "S-curve," as communities experiencing development pressure accumulate staff and regulatory obligations which remain in place long after development pressure has moved elsewhere in the region. This pattern can dampen developer interest in pursuing projects in established communities.

ZONED FOR COOPERATION: ORGANIZATIONAL TOOLS FOR DEVELOPMENT PROMOTION

Many of the barriers discussed earlier have their origins in restrictions on, or special powers granted to, various political subdivisions by State law. The effects of these barriers are potentially magnified by the unintended consequences of an organizational tool that was established by State law for the purpose of fostering collaboration between municipalities and adjacent townships: Joint Economic Development Districts (JEDD) and the Cooperative Economic Development Agreements (CEDA). The official, legal formalism of these entities contrasts sharply with the informal, more privately-driven models of the Special Improvement District (SID) and the Community Development Corporations (CDC) which are the principal organizational tools for championing infill and redevelopment. These mechanisms are described in detail below.

Joint Economic Development Districts and Cooperative Economic Development Agreements

Joint Economic Development Districts (JEDD) are authorized under Section 715 of the Ohio Revised Code which enables municipalities and adjacent townships to cooperate to foster economic development activities without modification of jurisdictional boundaries. A JEDD is a quasi-jurisdictional entity formed by cooperative agreement between a municipality and a township upon petition of 51% of the landowners comprising the proposed district. A JEDD provides an arrangement whereby municipal services—typically water and sewer—can be extended into one or more non-residential areas within a township. Municipalities can collect income tax from the township, in exchange for remitting a percentage of the tax revenues to the township and promising not to annex the township land on which the JEDD is formed for a minimum of three years.

The Cooperative Economic Development Agreement (CEDA) is authorized under Section 701.07 of the Ohio Revised Code and provides another mechanism by which municipalities and townships can avoid conflicts regarding annexation. CEDAs are less stringent than JEDDS: CEDAs enable communities to collaborate in the provision of infrastructure and public services and can include residential as well as non-residential properties. Unlike JEDDS, CEDAs do not permit the imposition of an income tax on the township.

JEDDs and CEDAs resolve several of the exogenous development barriers identified above. The appeal of this mechanism to both city and township is multifold. The municipal partner is able to shape and share in the benefits of development in an adjacent township and realize additional revenues by providing municipal water and sewer services while avoiding a protracted and costly annexation fight with that community. The hosting township is able to realize an intensity of new development which would otherwise exceed its capacity to support. JEDDs, in addition, allow townships to receive a portion of the of income tax revenue generated within the JEDD. These new revenues can enable the township to invest in higher-quality services or additional infrastructure to entice further retail or residential development. The JEDD also resolves concerns with limited township zoning and development review by vesting that power in an appointed board comprised of members designated by landowners, workers, and official representatives of the parties to the JEDD. This board typically undertakes a master plan study, which designates land use and zoning within the JEDD, clearly communicating intent to prospective developers.

JEDDs and CEDAs have proliferated in Northeast Ohio over the past decade as townships seek to expand and intensify development within their boundaries and adjacent municipalities seek to moderate the fiscal impacts of outward migration by shaping that development and sharing in its proceeds. Pioneered by Akron and Summit County (JEDD enabling legislation was championed by Don Plusquellic, Mayor of Akron and enacted in 1993) these inter-community cooperative agreements have reduced conflict between municipalities and adjacent townships and have fostered a measure of regional collaboration.

At the same time, by extending the region’s infrastructure footprint principally through the expansion of existing water and sewer networks, these agreements unintentionally—but undeniably—drive further outward migration of jobs and investment and add to the region’s long-term infrastructure maintenance burden.

An interesting case illustrating these dynamics unfolded fairly recently. The Eaton Corporation, long a resident of downtown Cleveland, decided in 2008 that it needed to move to a suburban campus to accommodate planned expansions and consolidations of corporate functions. The company identified a site in Beachwood, Ohio, on the eastern fringe of Cleveland in the Chagrin Highlands Corporate Park, with ready access to I-271 and close to a major new health care facility, the University Hospitals Ahuja Health Center. The Chagrin Highlands Corporate Park is located in a JEDD administered by the City of Beachwood in cooperation with Highland Hills, called the Beachwood East JEDD. The JEDD negotiated an agreement with the City of Cleveland whereby a percentage of income tax collected by the City of Beachwood would go to the City of Cleveland; in exchange for Cleveland selling land it owned to complete the site for the corporate campus. Highland Hills collects property tax. The parties reached an agreement and Eaton proceeded to build its new headquarters, completed in April 2013.

The Eaton headquarters case illustrates the potential for JEDDs, CEDAs and similar inter-community cooperative agreements to shift jobs and investment between communities, sometimes from the very same city that is a party to the agreement. In addition, by extending the region's infrastructure networks, these agreements have the potential to inflate the supply of greenfields commercial property in the region's market and further disadvantage infill redevelopment sites in the region's established communities As the scenario planning alternatives illustrate, the absence of robust tools to analyze the long-term fiscal impacts of expanding the region's infrastructure networks and polices that speak to mitigating these impacts exposes the region and its communities to the risk of incurring costs in excess of revenues over an extended period of time.

Special Improvement Districts and Community Development Corporations

Municipalities do not have nearly as expansive a set of tools for encouraging the development of their more established neighborhoods as they do for areas at their edge. Most of the fiscal tools available to municipalities discussed have profound limitations in their application and tend to compound administrative complexity. The dominant organization tool available to inner-city commercial districts, the Special Improvement District (SID), is not so much intended to function as a development instrument as a source of supplemental income to fund public services and special programs that the municipal government may not be able to otherwise provide.

SIDs were enabled by the State of Ohio in 1994 and permit area property owners to pay a dedicated property tax assessment to provide enhanced services to their district. These services are intended to strengthen the districts attractiveness and economic vitality by providing incentive programs and supplemental services that enhance and support—but do not replace—those normally provided by the city.

In the absence of a publicly-backed development district akin to a JEDD, non-profit community development corporations (CDCs) have emerged in many established Northeast Ohio communities to redress some of the endogenous redevelopment barriers and act as an intermediary between overburdened city governments, existing landowner interests, and prospective developers. Some of these organizations, like the Downtown Cleveland Alliance, have created a SID to assess themselves for physical investments in their public realm as well as supplementary services such as security, cleaning, and staff support for festivals and events. Others, like Midtown Cleveland, Inc., have remained entirely private voluntary organizations funded by their members. Yet others, such as Northeast Ohio's many neighborhood-based development corporations focus on affordable housing and small business development and fund their activities through a variety of public private partnerships.

A common thread in the experience of all community development corporations, and improvement districts, is the commitment to making "place" the distinguishing value proposition that attracts and retains people and jobs. The importance of place-making came up in multiple interviews: Interviewees felt that quality of place is increasingly important to the market. This response strongly suggests that policies emphasizing place-making will be of essential importance to the region's prospects for growth in jobs and residents.

CONCLUSION

There are formidable, structural drivers of outward migration and barriers to redevelopment, embedded in market characteristics, physical realities, the law, policy choices past and present, and industrial and political organization. Many recent strategies have been tested to overcome some of these barriers, including JEDDs, CEDAs, SIDs, and CDCs. JEDDs, in particular, have provided an effective means of generating new investment and development and fostering intra-regional collaboration. At the same time, this new investment and development, by definition, takes the form of outward migration and shifts economic activity away from legacy communities. Improvement districts and CDCs have made important contributions to making redevelopment more attractive, but critical market and policy barriers remain. Real estate trends indicate changing conditions that may make it easier to reverse the outward migration pattern, especially as consumer preferences shift to an attention to quality of place, but capitalizing on such trends will require thoughtful revision of public policy and openness to collaboration between governments, developers, and community partners.

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