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Commentary on Evan McKenzie, The Relationship Between the Rise of Private Communities and Increasing Socioeconomic Stratification

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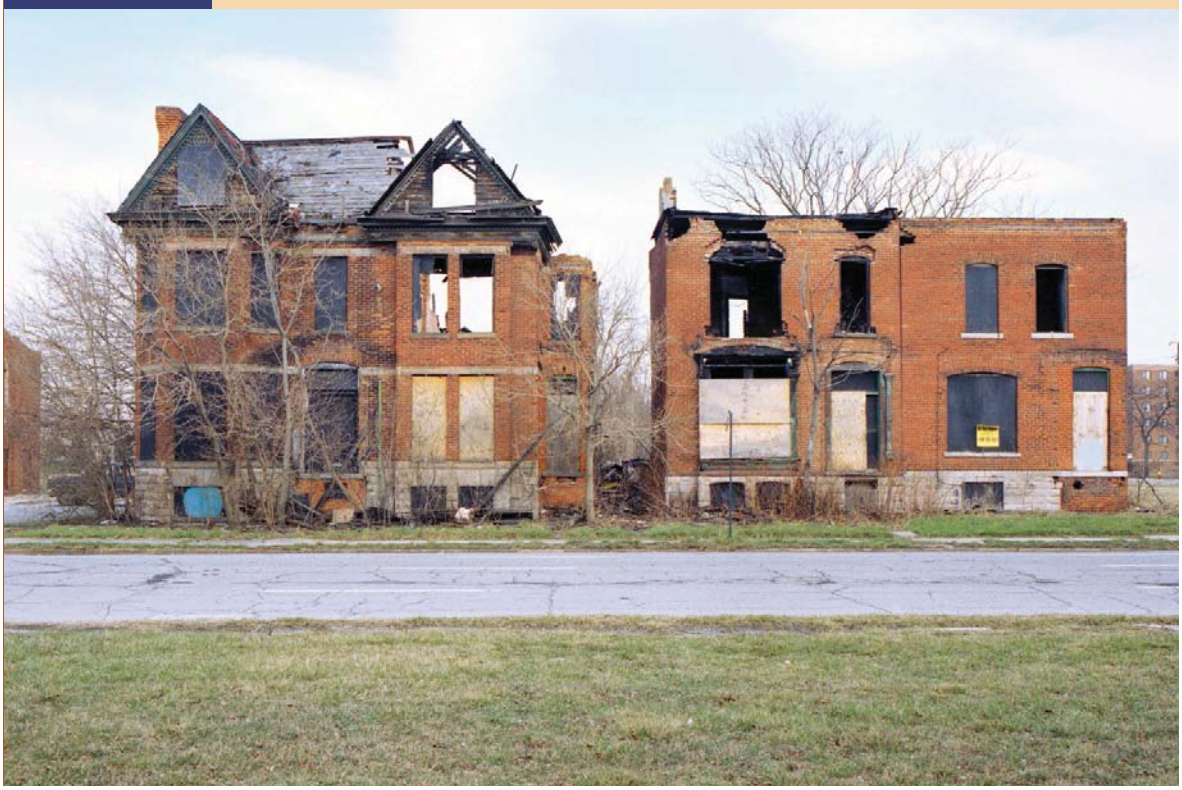
Land and the City

Edited by George W. McCarthy, Gregory K. Ingram, and Samuel A. Moody



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PREFACE

The majority of the world's population now lives in urban areas and depends on urban systems for housing and social and economic goods and services. This number will only increase as cities blossom and expand to accommodate new residents, particularly in developing nations. What remains unchanged, however, is the key role of cities as engines of economic growth, social activity, and cultural exchange. In an effort to support the success and sustainability of cities, this volume explores how policies regarding land use and taxation affect issues as diverse as the sustainability of local government revenues, the impacts of the foreclosure crisis, and urban resilience to climate change.

This collection, based on the Lincoln Institute of Land Policy's 2014 annual land policy conference, addresses the policies that underlie the organization, financing, and development of the world's cities. It is the final volume in the Institute's land policy conference series. Over the years, these meetings have addressed land policy as it relates to a range of topics, including local education, property rights, municipal revenues, climate change, and infrastructure.

We thank Armando Carbonell, Martim Smolka, and Joan Youngman for their advice on the selection of topics and on program design. The conference was organized by our exceptional event team, comprising Brooke Burgess, Sharon Novick, and Melissa Abraham. Our special thanks go to Emily McKeigue for her exemplary management of the production of this volume, to Peter Blaiwas for the cover design, to Nancy Benjamin for maintaining the publication schedule, and to Barbara Jatkola for her tireless and reliable copyediting.

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COMMENTARY
Gerald Korngold

In 1994, Evan McKenzie published the urtext on the rights of individual owners in homeowners' associations, *Privatopia: Homeowner Associations and the Rise of Residential Private Governments* (McKenzie 1994). In this chapter, he addresses the question of whether common interest developments (CIDs) have contributed to a general stratification of the housing market. After conducting a comprehensive and thoughtful analysis of the literature on the issue, he concludes:

> Ultimately, CID housing is a real estate development tool, an instrument of public policy makers, and an expression of individual consumer preferences. It can be used for exclusionary and segregative purposes. It can also be a vehicle for promoting inclusionary policies and practices that aim to house the middle and upper-middle classes in redeveloped urban neighborhoods. If we view CID housing as a tool, the responsibility for its impact on our society rests with developers, policy makers, and consumers alike.

Three further directions of inquiry may be helpful in exploring, if not implementing, McKenzie's conclusion. These involve data, normative issues, and legal considerations.

Data

Several of the existing studies do not seem directly related to the question of stratification, especially in the current climate. Investigations of gated communities can be misleading. While at times gates are powerful symbols of exclusion (and not so powerful when they enclose the entrance of a middle-income apartment building), actual exclusion is usually achieved through high homeowners' association fees arising from a high level of community amenities (annual exclusionary costs), as well as minimum lot size and building and architectural standards (acquisition exclusionary costs). It is these costs, not gates, that typically make CID housing unaffordable.

Further, deeper segmentation of the data is necessary to make real judgments about stratification. CIDs run the gamut from eight-figure oceanfront homes to middle-income housing cooperatives with caps on resale prices. Also missing in the studies are good numbers on the percentage of new homes built in CIDs versus those built outside them over the past several decades. These data would indicate whether consumers have meaningful alternatives and at what costs. Finally, demographic slicing based on the ages of CID owners is needed to understand the demand by millennials for such housing.

Normative Issues

Policy makers, courts, and legislatures are faced with competing normative considerations in deciding whether to address stratification and CIDs. Arguing against intervention by these entities are general laissez-faire ideas (CIDs represent free choices by individuals), the beliefs that CIDs are not uniformly "for the rich" and that our society tolerates wealth differences, and perhaps Tiebout theory. Arguments in favor of intervention are the belief that economic segregation in housing leads to poor outcomes in health, educational and employment opportunities, and housing value appreciation, among others.

Legal Considerations

Even assuming that policy makers believe that CIDs cause stratification, they may have only limited legal tools to address the situation. Importantly, while CIDs are created today pursuant to statutory authorization, in the past they were, and still can be, created under common-law principles.

The earliest cooperative apartments in New York City were ventures organized by the wealthy on Park Avenue, Fifth Avenue, and Central Park West, where cooperators pooled their cash and acquired buildings by utilizing standard corporate and landlord-tenant law. Subsequent legislation in New York State, such as the 1971 Banking Law that allows banks to grant mortgages on the security of cooperative shares and leases, have helped make these arrangements available to middle-class owners.

The common law could have been used to create the same legal structure as a condominium by employing air rights, easements, and covenants. Passage of condominium statutes across the country was necessary, however, to assure institutions lending to middle-class (and other) buyers of the legitimacy of such arrangements. The statutory authorization also avoids the need for expensive (and perhaps unaffordable) bespoke documentation that common-law arrangements would require. These statutes have helped democratize CID housing by validating financing and lowering transaction costs.

In other regards, state legislatures could prohibit subdivision covenants that directly exclude rental tenants because of the source of their payments, such as subdivision bans on renters participating in government rent assistance programs like Section 8 (Geggis 2014). These subdivision covenants discriminate between people with equal buying power, creating class discrimination as well as market distortions. While a full ban on renters represents a desire to have only those with long-term investments living in the community, distinguishing between tenants able to pay based on source of income smacks of class discrimination that a legislature may resist.

Moreover, state legislatures could theoretically address the stratification effects of CIDs through inclusionary zoning, assuming that there is the political will to do so. One type of inclusionary zoning requires mandatory set-asides of

affordable housing in new CIDs in exchange for land use regulatory approval. These mandatory provisions have been struck down by some courts, which have found them to be takings of the developer's property or violations of the equal protection or due process clause (Mandelker 2003). Given that only a few states have adopted set-asides that have survived challenges and that CID developers have significant political savvy, it may not be likely that many additional legislatures will impose such requirements on CIDs in the future. An alternative method of providing inclusionary housing is through incentive zoning, in which developers are given zoning benefits for setting aside affordable housing units. CID builders, however, may prefer not to utilize incentive zoning if they believe that the presence of affordable units will impact negatively on their sales and pricing of market-price homes. Moreover, even if a CID agrees to include affordable housing in order to obtain zoning incentives, stratification may not be alleviated, as the story about a New York City condo having a separate entrance for affordable housing tenants starkly illustrates (Briquelet 2013).

The power of local land use bodies to exact affordable housing in CIDs through the approval process is limited as well. Such power must trace to an overall legislative authorization, and as indicated above, such legislation might be subject to a variety of constitutional challenges. Moreover, U.S. Supreme Court decisions, from *Nollan v. California Coastal Commission* to *St. Johns River Water Management District v. Koontz*, have demonstrated sensitivity to the use of the exaction process to "extort" "improper" concessions from landowners.[1]

Judicial intervention may be similarly limited. It would be difficult to challenge minimum lot requirements within a CID on constitutional grounds, since there is no state action in the decisions of private owners to require certain lot sizes (Korngold 2004). As a result of such choices, however, many lower-income people might be unable to acquire property in the CID. Moreover, it is hard to imagine a theory under which judges could strike down high association fees to support CID amenities. Members have the right to contract freely (Korngold 2004); such a decision might force an association to default on its obligations to third parties (e.g., security companies); and even a public entity—a city—is free to offer whatever amenities (parks and the like) its residents want, and to assess corresponding taxes to pay for them. Under this reasoning, ongoing residency in a CID could remain unaffordable for many.

In sum, McKenzie has provided an important challenge to policy makers. This commentary suggests that more data are needed, a serious discussion of norms must take place, and legal solutions will not be easy to find even if there is a will to act.

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1. *Nollan v. California Coastal Commission*, 483 U.S. 825 (1987); *St. Johns River Water Management District v. Koontz*, 133 S. Ct. 2586 (2013).

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