The background of the entire page is a photograph of a construction crane on the left side, reaching upwards. The right side is dominated by the dense, green foliage of trees. The sky is a clear, bright blue with some light clouds. A semi-transparent white horizontal band is overlaid across the middle of the image, containing the main title and subtitle.

REDEVELOPING the **NORM**

Identifying and overcoming developer obstacles
to redevelopment in New Jersey



January 2016

REDEVELOPING the NORM

Identifying and overcoming developer obstacles

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EXECUTIVE SUMMARY

New Jersey is the most developed state in the nation. As of 2007, one-third of New Jersey's total land area was urbanized. Removing undeveloped lands that are not developable from the equation – either because they are environmentally constrained or have been permanently preserved – New Jersey had actually developed 60 percent of its buildable land by that time. And the state is still growing, even as it begins to run short of developable land. In order for population and employment growth to continue while preserving natural areas and farms, most future development will need to take place on previously developed sites. This means that redevelopment and infill development are the future of growth in the state of New Jersey.

There are indeed signs that such a shift toward redevelopment is taking place. For one thing, demographic and cultural shifts appear to be on the side of redevelopment, with the Millennial generation (those currently in their 20s and early 30s) souring on spread-out, car-dependent suburbs and choosing instead to live in more walkable, mixed-use centers. The rise of redevelopment has only gotten more pronounced since 2008, when a recession, housing market crash, and spike in gas prices combined to reset the calculus of households' tradeoffs between housing costs and transportation costs.

REDEVELOPMENT AND INFILL DEVELOPMENT ARE THE FUTURE OF GROWTH IN THE STATE OF NEW JERSEY.

Municipalities have much to gain by engaging in redevelopment. By making more efficient use of already developed land, towns can at the same time add to their tax base, preserve remaining undeveloped areas, eliminate vacant and/or antiquated buildings, bring new vitality to existing areas and for existing residents, add public amenities.

Nonetheless, in many parts of New Jersey, “greenfield” development – a term that generally refers to development on a site that has not been previously developed and which is located in a rural or low-density suburban context – too often remains the default model for developers and municipalities. How are greenfield and redevelopment projects different in the eyes of the development community and how can municipalities better understand these differences in order to encourage and support good redevelopment in their communities? This report seeks to answer these questions by drawing on the expertise of private real estate developers to compare the costs and risks of redevelopment projects with those of greenfield development projects and to identify areas where municipal officials can help mitigate some of the redevelopment-oriented risk and costs to spur good redevelopment.

There are many different risk and cost factors that a developer will weigh to decide whether to proceed with a project. Redevelopment projects and greenfield projects typically have very different risk and cost factors. The perception – and the reality in many cases – is that redevelopment projects come with added costs and risks. For example, the amount of time a project will take to complete is one of the factors a developer will consider when calculating risks and costs. Greenfield developments tend to move more quickly, thereby having a lower risk/cost associated with them, while redevelopment projects often take longer due to a variety of factors like land acquisition negotiations, zoning variances and the like. Land costs, another important developer consideration, tend to be higher for redevelopment projects because they usually involve negotiating with multiple landowners and involve greater complexity.

While no two redevelopment projects are alike, there are two important and distinctive types of redevelopment projects that this report identifies – those within “areas in need of redevelopment” and those that are outside of these areas. Projects taking places in “areas in need of redevelopment,” especially if the use of eminent domain is not required, can be less risky and costly and have a smoother public path than redevelopment outside these areas.

And while no two redevelopment projects are alike, no two developers or towns are the same either. The higher risks and costs encountered in redevelopment can be mitigated substantially when the local

AN EXPERIENCED REDEVELOPER AND A SUPPORTIVE HOST MUNICIPALITY ARE THE TWO MOST CRITICAL INGREDIENTS TO A SUCCESSFUL REDEVELOPMENT PROJECT.

municipality is organized, supportive and has the capacity to manage the redevelopment process. Similarly, individual developers have varied levels of experience in redevelopment and in partnering with municipalities in the process, which affects individual risk calculations, cost containment and success rates. An experienced redeveloper and a supportive host municipality are the two most critical ingredients to a successful redevelopment project.

Saving time translates into saving money for the developer, which in turn makes the project more financially feasible. This is why the key to a project’s success is an organized and engaged municipality that gets out in front of the risk and cost factors it can control.

INTRODUCTION

There exists a great deal of empirical and anecdotal evidence that for the past 50 years greenfield development has been the preferred form of development for the real estate development industry. The perception in most markets is that greenfield development is more predictable and costs less, and therefore is more profitable than redevelopment.

The purpose of this report is to identify both real and perceived issues that have slowed the development community from engaging more fully in redevelopment projects as compared to greenfield projects. The approach is twofold: 1) To identify areas where cost and risk factors make redevelopment projects more challenging than greenfield projects, and 2) To communicate to municipalities some of the existing barriers that prevent or impede developers from engaging in redevelopment and to show how a municipality can help lower these barriers and risks while still achieving the town's quality and growth goals.

FOR THE PAST 50 YEARS GREENFIELD DEVELOPMENT HAS BEEN THE PREFERRED FORM OF DEVELOPMENT FOR THE REAL ESTATE DEVELOPMENT INDUSTRY.

GREENFIELD DEVELOPMENT VS. REDEVELOPMENT

The term *greenfield* refers generally to development on a site that has not been previously developed (in other words, has not been paved over or had structures built on it) and which is located in a rural or low-density suburban context. However, the term does not necessarily imply that the land being developed is in a “natural” state, since often the development is on a site previously used for agricultural purposes. The term also carries the connotation that the development site is located at the edge of or outside of an existing urbanized area.

Redevelopment is generally defined as development on a site that had been previously developed with infrastructure and

buildings. This includes abandoned or underutilized commercial, residential or industrial properties, usually in a suburban or urban community. It also generally includes vacant lots resulting from structures having been demolished.

Infill development is the development of smaller vacant parcels of land that, while located within a built-up area and surrounded by developed parcels, may or may not have been previously developed. Infill has many of the same attributes as redevelopment, and confronts many of the same obstacles, but was not specifically analyzed during this study.

IMPORTANCE OF REDEVELOPMENT

New Jersey continues to grow, and at the same time is running out of developable land. As of 2007, one-third of New Jersey's total land area was urbanized.¹ When undeveloped lands that are not developable – either because they are environmentally constrained or have been permanently preserved – are removed from the equation, New Jersey had actually developed 60 percent of its buildable land as of 2007. What's worse, new development has gotten more land-hungry in the last several decades. In 1986, New Jersey had approximately 0.16 developed acres for every resident. Between 1986 and 1995, it added 0.27 newly developed acres for every new resident. This dipped slightly to 0.25 acres for the 1995-2002 period (though still well above the pre-1986 baseline), but increased to 0.64 newly developed acres per new resident between 2002 and 2007.

The looming prospect of full build-out has so far done nothing to dampen the consumption of developable land. Build-out is indeed looming: If the rate of 0.64 newly developed acres per new resident for the 2002-2007 period were to persist into the future, New Jersey's remaining million acres of still-developable land (as of 2007, the most recent year for which land-development data are presently available) would accommodate only about an additional 1.5 million people – less than New Jersey's population growth since 1970 – before every acre of buildable land had been built on. And that is before factoring in any additional preservation that takes open land off the market.

While many view the post-2008 recession as a period of reduced economic growth, the opposite occurred in terms of population growth. New Jersey’s total statewide population grew by only 1.46 percent from 2002 to 2007 according to Census Bureau estimates, but grew by 2.15 percent from 2007 to 2012.

For New Jersey to continue to add people and businesses while preserving natural areas and farms, growth is best directed to previously developed sites that are currently abandoned or underutilized — that is, redevelopment sites. Fortunately, absorbing new growth on already-developed land is eminently possible. To take a simple example, there are 236 municipalities in New Jersey that had fewer residents in the 2010 Census than they had at some point in the past, with the total deficit over all 236 amounting to more than half a million. That is to say, if all of these municipalities were repopulated back to their maximum populations, the population of the state could increase by more than half a million people without the need to develop any additional land.

DEMAND FOR REDEVELOPMENT GROWING, BUT NOT YET THE DEFAULT

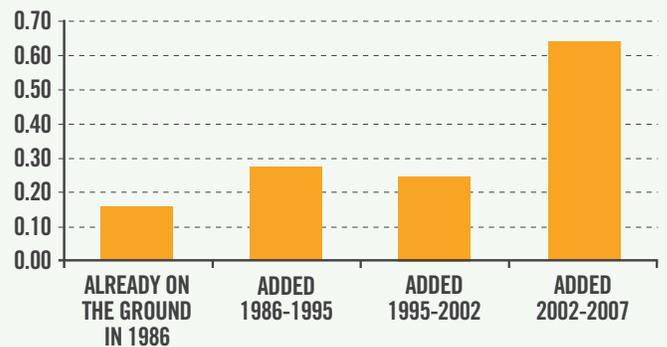
There are indeed signs that such a shift toward redevelopment is starting to take place. For one thing, demographic and cultural shifts appear to be on the side of redevelopment, with the Millennial generation (those currently in their 20s and early 30s) souring on spread-out, car-dependent suburbs and choosing instead to live in more walkable, mixed-use centers. They are walking more and driving less: “The US National Household Travel Survey, conducted by the Federal Highway Administration, found that average vehicle miles travelled by 16- to 34-year-olds fell 23 percent – to 7,900 miles – per capita between 2001 and 2009. Between 2000 and 2010 the percentage of US 14- to 34-year-olds without a driving license increased from 21 to 26 percent.”²

In New Jersey, a 1998 revision to the building code for rehabilitating existing buildings has helped spur new growth in many already-built places³ that had long been stagnant. As a group, the 204 municipalities that were already at least 90 percent built out as of 2002 issued 2.7 times more building permits in the 2000s than in the 1990s and more than doubled their

combined share of total statewide building permits issued, from 15.1 percent in the 1990s to 33.6 percent in the 2000s.

The rise of redevelopment has only gotten more pronounced since 2008, when a recession, housing market crash, and spike in gas prices combined to reset the calculus of households’ tradeoffs between housing costs and transportation costs, making cities and older, closer-in suburbs suddenly seem like a better deal. The 271 municipalities that were at least 90 percent built out as of 2007 together accounted for 54.5 percent of the state’s total population growth from 2008 to 2012, compared to only 3.6 percent of the total between 2000 and 2008. The older cities and boroughs in this group include such places as Garfield, Hackensack, Belleville, Bloomfield, Montclair, Bayonne, Weehawken, Clifton, Passaic, Cranford, Linden, and Plainfield. Many of these places had been stagnant or even losing population for decades before experiencing their revivals in the later part of the 2000s. These reversals of fortune come on top of the more widely-observed revitalizations that were already well under way in Jersey City, Hoboken, and New Brunswick and which gained steam in the

Figure 1. Trend in Developed Acres Per Capita



Development has gotten much more land-consumptive in recent decades. In 1986, 1.2 million acres of land in New Jersey had been urbanized, or about 0.16 acres for every resident. But between 2002 and 2007, an additional 0.64 acres were developed for every new person added to New Jersey’s population -- four times the amount of developed land per person that was already on the ground in 1986.

Sources: U.S. Census Bureau (population data) and Geospatial Research Laboratory at Rowan University (developed acres data)

later part of the 2000s: Hoboken's population grew by a remarkable 10.2 percent just between 2008 and 2012, while Jersey City's grew by 5.0 percent and New Brunswick's by 4.0 percent, compared to statewide growth of only 1.8 percent over the same period.

This is not to say that sprawl is yet a thing of the past, however. As mentioned earlier, between 2002 and 2007 New Jersey developed an additional 80,000 acres (about the size of all of Essex County), which amounts to 0.64 acres for every new resident it gained and four times the number of acres per person that had been developed up to 1986. This represented a 5.5 percent increase in New Jersey's developed acreage in that five-year period for just a 1.5 percent increase in population. It is true that since the recession, New Jersey has accommodated much more population growth via redevelopment than had been the pattern in the past, which has likely slowed the per-capita rate of land consumption since 2007. But many sprawling suburban counties are still gaining population in the same low-density places as before, just more slowly.

Thus for much of New Jersey, greenfield development remains a popular and in some cases preferred model. The counties in which developed acreage increased by the largest percentages from 2002 to 2007 were all at the fringes of the state's urbanized territory: Gloucester, Atlantic, Sussex, Warren, Ocean, and Hunterdon. In all of these counties, developed land increased at least 40 percent faster than population, in some cases more than twice as fast.

OUR APPROACH

During the spring of 2012, New Jersey Future and Monmouth University's Kislak Real Estate Institute collaborated to conduct research on built greenfield and redevelopment projects in the state of New Jersey. The research focused on the private real estate developers who are responsible for moving the majority of residential and commercial projects from concept to completion. To gain access to key industry data, the researchers recruited volunteer participants from New Jersey-based development companies that have extensive experience with a variety of developments throughout New Jersey. The research was conducted solely with mid- to large-size real estate developers with significant experience in New Jersey redevelopment and/or greenfield development. Participants provided information on specific New Jersey projects where they had direct involvement.

An initial survey instrument was developed to provide a consistent framework for questions. All participants received this survey prior to being interviewed. The survey and interview were designed to gauge the participant's level of experience, preference between redevelopment vs. greenfield projects and the cost and risk factors of specific projects. One of the goals was to collect enough information about individual projects in each context in order to analyze and identify significant cost differences between the redevelopment and greenfield projects; however, early on in the data-gathering process it became apparent that this was not feasible. Each development had so many unique, site-specific issues that the comparisons would not be meaningful. This was true especially for redevelopment projects.

Because of this, the interviews pivoted away from a line-by-line comparative cost analysis toward an assessment of the significant cost and risk factors that help drive developers to choose redevelopment vs. greenfield projects. The survey then became a guide for the interviewer to use in order to delve deeper into the quantitative and qualitative cost and risk levels in different types of developments, in order to understand better what motivates participants to pursue certain developments and not others.

The study identified cost factors using the traditional development budget categories of land, hard costs and soft costs. Additional third-party research was conducted to develop working explanations of specific cost elements.

After the costs were analyzed, a risk assessment was developed. The risk assessment identifies and explains common risk categories in real estate development projects, compares redevelopment and greenfield project risks and then explains risk factors further using weighted values and incorporating the impact of time and delays.

Finally, the report highlights reasonable ways that the development industry has identified to reduce costs and mitigate risk. Many of these suggestions involve government actions, some at the state level and some at the local level. The municipal actions are particularly instructive, as they identify ways that municipalities and developers can partner effectively to create win-win projects, especially while redeveloping areas that have been previously developed.

COST FACTORS

As part of the research project, budgets for multiple completed developments in New Jersey were reviewed. Due to the unique facts and circumstances of each development, line-by-line comparisons did not prove feasible. However it was possible to identify key expenses that had a significant impact on each development budget; to analyze the factors driving those expenses; and to identify the percentage range accounted for by these expenses in a project budget.

ACQUIRING PROPERTY FROM A SINGLE OWNER, AS IS TYPICAL OF GREENFIELD DEVELOPMENT, TENDS TO BE MORE STRAIGHTFORWARD AND INCREASES THE LIKELIHOOD THAT THE DEVELOPER AND LANDOWNER CAN COME TO AN AGREEMENT.

Development budgets typically consist of three cost categories: land costs, hard costs and soft costs. Within each category, there are line items that make up a significant part of the overall costs of the development, including the land itself, permit and municipality fees, financing fees and interest (including both land and construction financing), environmental clean-up, and building construction costs. Each of these key expenses is not unique to a greenfield or redevelopment project; greenfield and redevelopment projects tend to share the same types of expenses, but differ in the percentage that each makes up within the overall budget. For example, a greenfield may have some environmental remediation but it may be a smaller percentage of the overall budget than the remediation in a highly contaminated redevelopment site's budget.

The following analysis looks at significant cost factors in greenfield and redevelopment projects using the three budget categories of land costs, hard costs and soft costs.

LAND COSTS

Land costs include the cost of the land itself and all financing costs associated with acquiring the land (if applicable). Based

on the budgets reviewed, land costs ranged from as high as 25 percent of the total development cost to as low as 6 percent. In most developments there is little room to negotiate hard and soft costs, so developers typically look at land costs as the “plug;” that is, the remaining amount that can be spent after hard and soft costs and projected profit are subtracted from a projected sale or lease price. This puts significant pressure on the developer to buy the land at the right price.

Land acquisition for greenfield development can be less difficult than for redevelopment since it usually involves negotiating with fewer land owners. Acquiring property from a single owner, as is typical of greenfield development, tends to be more straightforward and increases the likelihood that the developer and landowner can come to an agreement. Conversely, in redevelopment, land is usually in small parcels and owned by multiple people. This increases the chances that one person (or more) may hold out and not want to sell his or her land to the developer. This makes it far more difficult to assemble and acquire all the needed land. This is one of the most significant disadvantages that redevelopment has versus greenfield development. Land assemblage efforts can take years and are not guaranteed to result in the developer acquiring all the needed parcels. Furthermore, the additional effort required of the developer to obtain all of the needed land and negotiate with multiple parties can cause the developer to overpay for the land or walk away from the development entirely.⁴ Municipalities that have declared areas in need of redevelopment, using eminent domain or not, have increased tools at their disposal to help assemble and package sites for a redeveloper.

Land in areas that are formally designated by the municipality as “areas in need of redevelopment” will typically have the advantage of preferential zoning (such as higher density) having already been adopted via a redevelopment plan. This is due to the fact that the municipality is seeking to advance redevelopment and is attempting to make the guidance and requirements more favorable for development, and in many cases more flexible. This is not the case with greenfield developments or even in redevelopment areas that have not gone through this municipal process; therefore the developer must work through zoning issues.

HIGH-RISE STRUCTURES ARE TYPICALLY THE MOST COSTLY, SINCE THEY REQUIRE THE USE OF CONCRETE AND STEEL CONSTRUCTION, WHICH INCREASES BOTH MATERIAL AND LABOR COSTS SIGNIFICANTLY.

A developer will need to have site control before they move through the time and cost-intensive process of obtaining land entitlements, such as necessary zoning. To minimize initial acquisition costs, the developer may look to use a purchase option agreement with the seller that will allow the developer the option to buy the land subject to certain conditions, such as the developer's ability to obtain the desired zoning and the other governmental approvals required to commence construction. Under such an agreement, the developer would not complete the purchase of the land until the zoning is in place. This purchase option agreement not only mitigates the developer's exposure to zoning risk, it also minimizes the developer's initial financial commitment. Because the developer has the option to acquire the land but is not required to, the developer pays the landowner a recurring fee that is typically much smaller than the cost that the developer would pay to acquire the land outright.⁵ This is not always an option when trying to assemble multiple parcels.

The purchase option also benefits the landowner. It puts on the developer the financial burden of getting the land entitled. Furthermore, the land value will increase based on the developer successfully obtaining the desired entitlements. In most greenfield land sales, the sale price of the land is dependent on the number of units or square footage for which the development gets approved. Thus, zoning with higher density or Floor Area Ratio (FAR) will allow the landowner to sell the land for a higher price to the developer.

HARD COSTS

Hard costs typically include amounts for site preparation, environmental cleanup, labor, materials, improvements and contractor fees. Of these costs, the most significant can be environmental cleanup, material, labor and improvements. In the budgets reviewed, hard costs were as high as 79 percent of the total budget and as low as 56 percent.

While hard costs are negotiable with individual contractors, the marketplace is competitive and prices for similar work do not vary significantly. Prices do vary based on the size of the project and type of construction. High-rise structures are typically the most costly, since they require the use of concrete and steel construction, which increases both material and labor costs significantly. To maintain the development's economic feasibility, the increase in cost is mitigated with higher density and, if market conditions permit, a shorter lease-up or sales period.

If market conditions are not as favorable, the developer may choose to delay commencement until the market is more favorable, or may look to build a smaller, non-steel mid- to low-rise building. The smaller structure would be built using "bricks and sticks," making it less expensive to build and typically allowing for more flexible labor arrangements. This would hold down costs, maintain reasonable density, still fit the market and keep the project economically feasible.

In a greenfield development, zoning is typically lower-density than in redevelopment. As a result, the nature of greenfield developments tend to be smaller and more spread out with multiple structures resulting in two- to four-story wood-frame buildings. This type of construction is the least expensive, low-complexity and it has the most flexible labor arrangements. Also, the nature of this type of project allows the developer to split the development into phases. This gives the developer the opportunity to start selling or renting the first completed phases before all phases are finished, as opposed to a large high-rise development that must be 100 percent complete prior to selling units or collecting rent. This is another benefit to the typical greenfield development; helping to provide the developer cash flow earlier in the development.

Unfortunately, there isn't much that the developer can do to reduce hard costs of a development short of reducing quality, which is a genuine concern, especially when buildings are an integral part of the community fabric. The best that developers can do to manage hard costs is focus on creating an accurate budget, operate efficiently, reduce waste, and monitor the budget regularly. Also, developers can reduce their exposure to budget overruns by negotiating construction guarantees from the general contractor performing the work. This allows

Why do **COSTS** matter?

Developers conduct initial feasibility assessments when deciding to proceed with a development opportunity. To be feasible, the projected revenue from the project must exceed the projected costs of the project, allowing for a fair profit. The costs to deliver different types of projects in different locations can vary significantly. Types of projects and places that consistently have greater costs will require stronger markets and higher rents or sales prices in order to be feasible.

developers to agree contractually on a building cost early in the process so that they can focus their attention on managing other risks of the development.⁶

SOFT COSTS

Soft costs are not physical items; they are intangibles. They include the interest, financing fees, architectural, engineering, permit and municipal fees, legal, and marketing etc. Of these costs the most significant tend to be financing fees, interest, permits and municipal fees. From the budgets reviewed, financing fees, interest, permits and municipal fees were as high as 16 percent and as low as 6 percent of the total budget. Total soft costs were as high as 33 percent and as low as 14 percent of the total budget.

Loans are typical in developments because the majority of the costs associated with a development are financed through a lender and equity partner. The amount of debt is typically as high as 75 percent or as low as 50 percent of the total costs. Lenders are not always willing to finance certain costs in a development, but a loan package is based on many factors and therefore can vary. For example, a lender may provide a construction loan that will cover 50 percent of the land, 100 percent of hard building costs (including site preparation), 100 percent of interest reserve (with conditions), and 0 percent of soft costs (excluding interest reserve).⁷ Lending institutions do not like to finance soft costs because often these costs don't add value to their collateral. This is not the case with all lenders and it is very much dependent on the borrower, but banks try to protect themselves in the event of default. For example, a bank could recoup some of its loan if it is spent on a concrete foundation, but it may not recoup funds loaned for legal fees to get plans approved or land rezoned. For this reason banks will typically expect the developer's equity to be used on most of the upfront development soft costs.⁸ In addition, since the economic downturn and concerns over the viability of many

banks, regulatory changes further limit the ability of many banks in making development related loans.

This puts pressure on both greenfield and redevelopment projects. Many greenfield projects will not require rezoning, which will reduce this expense. Greenfield developments that require the land to be rezoned will generate soft costs that must be borne by the developer. The preapproved preferential zoning and plans in redevelopment projects are sometimes not in line with current market demands; for example, an area in need of development plan may require significant retail when there is no demand for retail. Thus the developer will need to bear the financial burden of getting the land rezoned and new plans approved to meet the current market realities, but differ from the redevelopment plan. The professional fees spent on rezoning and getting plans approved can be significant. If market conditions are not favorable and a municipality is not flexible, the professional fees can quickly cause a development to become unfeasible.

Financial fees and interest make up a significant part of soft costs. From budgets reviewed, they averaged 26 percent of total soft costs. These costs are heavily dependent on how much time it will take to complete the development. The longer it takes to complete the development, the higher the financial costs. This puts redevelopment projects at a disadvantage since they typically have a very long timeline. A disproportionate amount of a redevelopment project's budget must be allocated to financing costs, which puts increased pressure on the project's economic feasibility. Conversely, a greenfield development will have less of its budget allocated to financial costs and therefore less pressure on its economic feasibility.

RISK FACTORS

Eleven categories of risk were identified as being important in the development decision-making process. These risk factors are cumulative. The greater the cumulative risk associated with a project the less likely it is to be selected by a developer as a place to invest time and capital.

All risk factors are not treated equally. While we present a scientific look at risk, including the weighting of risk and the impact of time on risk, each developer will assess the importance of each risk factor and the magnitude of risk tolerance for each factor on a case-by-case basis.

REDEVELOPMENT PROJECTS ARE LOCATED IN PLACES THAT ALREADY HAVE INFRASTRUCTURE; HOWEVER, THE RISK IS THAT THIS INFRASTRUCTURE IS NOT ADEQUATE TO SUPPORT THE DEVELOPMENT AND WILL NEED TO BE REPAIRED, UPGRADED OR REPLACED.

During the course of this study, it became evident that there were two very different types of redevelopment projects and that this distinction had a direct and material effect on several risk categories. For the purposes of the following risk analysis, redevelopment projects are divided into two categories: 1) “big-R” redevelopment projects that are located in officially-designated redevelopment areas and are consistent with formal municipally adopted redevelopment plans and 2) “little-r” redevelopment projects that involve the development of sites previously developed, but without any formal area designation. The analysis will review these two types of redevelopment projects alongside greenfield developments.

CATEGORIES OF RISK

Each of the three development types (two redevelopment – big-R and little-r, plus greenfield) has similar categories of financial and non-financial risk. However, each development type may not have the same amount of risk associated with

each category. As risk factors accumulate, developers will need to project higher expenses, realign revenue projections or build in a larger profit margin to account for them. As these risks increase, the feasibility of the project decreases and the likelihood of the project being built fades. The following outlines the eleven key categories of risk, highlights some distinctions among project types, describes weighted risk and then demonstrates risk over time.

Entitlement – whether it will be possible to obtain government approvals, including zoning and planning board approvals, to develop. Because of the extensive front-loaded process of creating a municipally-approved redevelopment area and plan that includes what the community will and won’t allow, the government approval process is often less risky for big-R redevelopment projects. While greenfield projects don’t have this benefit, developers will often be able to make marketable projects fit within the existing zoning and entitlement structure. If not, the risk can be high. Little-r redevelopment projects typically have the most difficult time, since the existing zoning and entitlements have usually been in place for a long time and may no longer support the dynamics of the current marketplace.

Construction – whether it will be possible within budget to design and build what was originally proposed. Redevelopment projects typically require more individualized design and construction practices, which can increase risk. Mid-rise and high-rise developments and their associated requirements for structured parking cost more on a per-square-foot basis and can also carry higher risk. By contrast, greenfield development is a mature industry and the cost factors for standard construction are well known and understood by experienced developers and lenders. Given constrained sites and working within the built environment, redevelopment can be more challenging and expensive for staging and logistics of construction.

Market – whether it will be possible to sell or rent a development project at price points that will produce the projected revenue levels in a timely way. This is always a significant factor. Pre-selling or leasing helps reduce this risk. Understanding and predicting sales and rental prices and absorption

HAVING A MUNICIPALLY ADOPTED REDEVELOPMENT PLAN CAN MAKE GETTING ZONING AND BUILDING APPROVALS EASIER.

(how fast units can be rented) in weaker markets, where many municipalities would like to see redevelopment, is more challenging and creates tighter financial margins and more risk. Changing demographic conditions that favor more walkable and compact communities, especially near transit, are increasing demand for redevelopment sites and projects in these locations and thereby reducing market risk.

Environmental – whether it will be possible to identify and remediate within budget all environmental issues. Assessing and cleaning sites to developable standards is not only a significant cost factor, it also can be unpredictable since contamination can be uncovered incrementally during the development process. Redevelopment sites often have a higher environmental cost factor as well as risk factor, though greenfields can also have environmental-cleanup costs, especially when developing previously farmed land where chemical pesticides and fertilizers have been used, like orchards.

Natural Constraints – whether it will be possible to develop the project without interfering or being constrained by natural features. Greenfield sites by definition are designed and developed in places that have not been developed previously and therefore typically have more natural constraints that need to be addressed in the design process. These constraints can include steep slopes, wetlands, existing surface water bodies and impervious surface issues. Conversely, redevelopment sites have few of these natural constraint issues; however, they do pose opportunities for restoring or improving previously damaged natural features or systems. The regulatory structure in New Jersey encourages developers to avoid natural features or spend a great deal of time and money mitigating encroachments.

Land Assemblage – whether it will be possible to acquire the necessary parcel or parcels in a timely way at an acceptable cost. Greenfield sites are typically purchased by a developer from a single owner, which makes the assembly of a developable site very predictable. Redevelopment projects typically involve the developer needing to acquire multiple sites from unrelated owners. This process is not only time-consuming but highly unpredictable, since just one of those owners can prevent the necessary assembly of project parcels. The

multiple-ownership issue can also make the eventual land-acquisition price for the whole project very unpredictable and in some cases more expensive than projected as the final pieces are pulled together.

Financial – whether it will be possible to get quick and favorable financing to meet the needs of the project. Financial institutions are more accustomed to the risk and development schedule associated with greenfield projects, and therefore can offer better terms, faster approvals and better access to capital, but this is starting to change. Many larger developers are greenfield developers and have developed the internal capital or partnership structures either to self-finance or to reduce significantly the role of third-party lenders. Due to the more individualized nature of redevelopment, access to capital can be more difficult and time-consuming. Fewer well-capitalized developers are currently engaged in redevelopment, which means fewer mainstream lenders are developing a comfort level and expertise with redevelopment projects, which perpetuates the cycle of projects having fewer options and a more difficult time getting financing. This is especially true of mixed-use developments that contain residential and commercial uses.

Infrastructure – whether it will be possible to build or repair infrastructure that supports the project as well as the unpredictability of relying on third parties to deliver the infrastructure. Greenfield projects typically need to build the sewer, utility and road infrastructure necessary to support the new development. The costs can be significant and the scope can change during the course of the development. The risk lies in assessing accurately the scope of the project and the site conditions that the developer will face. Redevelopment projects are located in places that already have infrastructure; however, the risk is that this infrastructure is not adequate to support the development and will need to be repaired, upgraded or replaced. Coordination among owners of existing infrastructure adds additional uncertainty and time

to redevelopment projects. Infrastructure repair or replacement in redevelopment areas can require government to fund or to do the work itself. Alternatively, a lead developer may do the work and pay for it and require the assistance of government to establish an equitable repayment method from later developers who benefit from the infrastructure installed by the first developer.

Affordable Housing – the uncertainty surrounding how much affordable housing to include in residential projects. New Jersey requires municipalities to provide a certain amount of affordable housing for families with low and moderate incomes. The disruption in the state’s affordable-housing governance system and the resulting uncertainty faced by municipalities creates uncertainty for developers and redevelopers about their obligation to provide lower-cost housing units or pay fees to the town to cover the cost of providing units elsewhere. This issue increases risk across all development types.

Community Opposition – the risk that the community will slow or stop projects or layer on new costs. If a project is following the existing zoning, as in many greenfield developments, community opposition can cause delays but not stop the project. If variances are required, community opposition can kill a project. Greenfield projects oftentimes face the biggest local opposition because the community is generally surprised by the proposal, and a large-scale development proposal can mean big changes for a community. Big-R redevelopment projects can encounter both extremes. If the potential use of eminent domain is a factor, community opposition can be fierce and kill projects. Where eminent domain is not a factor, the municipality already has a community-approved plan and projects can move through with community support. However, in all redevelopment projects there will likely be a larger number of neighbors affected by the development and therefore the potential for larger-scale community opposition is high. Engaging the community early in the process can help turn opposition into support.

Uncertainty – Overall, the more uncertain and unpredictable the process is, the more risky the project. Redevelopment projects often carry more uncertainty because they involve more stakeholders and more issues that cannot be predict-

ed accurately at the beginning of the process. Because of this, redevelopment projects often take longer. Increasing the time frame to complete a project further increases the uncertainty around whether the project can meet its objectives within its original budget.

WEIGHTED RISK

For illustrative purposes, the preceding risk factors were analyzed using the External Factors Analysis Summary (EFAS) developed by Wheelen and Hunger.⁹ The EFAS is a strategic analysis tool used to help a business analyze how well they respond to their external environment. Although it is subjective, the EFAS provides a means of quantifying the different risks on a relative basis and to assess the resulting impact on a project in total. This framework also allows for a standardized and comparable approach in reviewing different types of developments.

**ENGAGING THE COMMUNITY EARLY
IN THE PROCESS CAN HELP TURN
OPPOSITION INTO SUPPORT.**

In the following section, the risk factors are weighted and the results are compared across the three development types identified as: (1) big “R” redevelopment, (2) little “r” redevelopment, and (3) greenfield. First, each factor was assigned a number value between 1.00 (most important) and 0.0 (least important). This number was used to weight each factor’s importance to the overall development, *relative to other factors*. The values assigned to all factors must sum to 1.00. These factors were assumed to remain constant across all three types of development. Next, each factor was assigned a number based on the degree of impact that it would have on each type of development – high or 6, medium or 4, and low or 2. With the weighted value of each factor and its rated impact on the development, a score and a rank were created for each development type. See Figure 2 for details.

Why does **RISK** matter?

When a developer is conducting a project feasibility assessment, it is important to assess the risk associated with each set of projections and with the project itself. The greater the risk, the larger the margin (aka “risk premium”) a developer will need between anticipated revenues and expenses. If that margin cannot be increased to account adequately for the risk, the project will not be feasible. Developers can attempt to mitigate risk factors, but many of these are outside of their control. When the risk factors cannot be reduced sufficiently, the project will be rejected.

The risk factor weights were selected by the researcher and based on interviews with developer participants and on secondary research. These weights are not intended as a statistically defensible weighing of risks, but rather to generate a picture of how different individual factors influence the overall risk and cost of a project. Generating more objective and defensible weights would require additional research and analysis that is outside of the scope of this study.

Based on the results of the weighted risk factor in Figure 2, little-r was identified as having the highest weighted risk score, big-R the second highest, and greenfield the lowest. In general, these results are consistent with what was expected.

RISK OVER TIME

As the factors that cause risk are resolved, the overall project risk goes down. Projects for which it takes longer to remove risk factors will remain at higher risk longer, making them overall more risky. Different risk factors tend to get resolved at different stages in a project’s life cycle, depending on the type of project. The various milestones and the risks that are most prominent at each point in time are described in detail below.

Commencement – The first milestone is the commencement of the development and is just the beginning of the process. At this point, each development starts with its beginning weighted risk score and is at its highest level of overall risk.

All Approvals – As the development receives the necessary approvals, certain factors drop from the development’s weighted risk score: entitlement, land assemblage, infrastructure, affordable housing, and community opposition. These factors are resolved as the municipality approves the developer’s

plans, the developer closes on the land, needed infrastructure gets determined and approved in the plans, affordable housing requirements are determined and included in the budget, the opposition (if any) does not prevent the developer’s plans from getting approved after it has exhausted all appeals.

10 to 18 Months – At this point, enough time has elapsed that some greenfield developments could be complete or near completion. Environmental and natural constraints have been incorporated into the project and cease to be risk factors. Within 10 to 18 months after commencement, the developer will have remediated any environmental contamination and likely received a Remedial Action Outcome (RAO) letter. In most cases, the developer has also had enough time to complete the land/site preparation work.

**AS THE FACTORS THAT CAUSE RISK ARE RESOLVED,
THE OVERALL PROJECT RISK GOES DOWN.**

2 to 3 Years – At this stage construction on the typical greenfield development would have been completed, and the developer will have sold/leased the property and moved on to a new development. If the greenfield development was built and sold, the developer would no longer be exposed to market risk, financial risk or uncertainty. However, if the project was rental, there would continue to be exposure to these risks since the developer would still own the project, but at different levels than a development project coming out of the ground. For big-R, little-r and more complex greenfield devel-

opments, the typical risk factors remaining are construction, market, financial, and uncertainty. These factors will remain until completion of the development.

2 ½ to 4 years – This is the first point at which a redevelopment can be complete. If not completed, the four remaining factors mentioned in the previous paragraph are still present.

6 plus years – At this stage, complex or large redevelopments will be completed or near completion. However, it is worth noting that some redevelopment projects can take well in excess of six years to complete. These projects likely take longer because of delays at the earlier stages previously discussed or the overall scale of the project.

Figure 2. Development Risk Factors Have Different Implications for Different Types of Development / Redevelopment Projects

FACTOR	DESCRIPTION	WEIGHT	BIG - R REDEVELOPMENT		LITTLE - r REDEVELOPMENT		GREENFIELD	
			IMPACT LEVEL	WEIGHTED SCORE	IMPACT LEVEL	WEIGHTED SCORE	IMPACT LEVEL	WEIGHTED SCORE
ENTITLEMENT	Obtain applicable local, county, state and federal approvals	0.150	Low-2	0.30	High-6	0.90	High-6	0.90
CONSTRUCTION	Manage construction to stay within budget	0.030	Med-4	0.12	Med-4	0.12	Low-2	0.06
MARKET	Level of consumer demand for development and factors that affect demand	0.150	High-6	0.90	High-6	0.90	High-6	0.90
ENVIRONMENTAL	Land contamination and remediation	0.100	High-6	0.60	High-6	0.60	Low-2	0.20
NATURAL CONSTRAINTS	Topography, proximity to natural resources (e.g. wetlands, streams etc.)	0.050	Low-2	0.10	Low-2	0.10	Med-4	0.20
LAND ASSEMBLAGE	Ability to acquire the needed land for the development	0.100	High-6	0.60	High-6	0.60	Med-4	0.40
FINANCIAL	Access to capital and wherewithal to cover the cost of capital	0.125	High-6	0.75	High-6	0.75	Med-4	0.50
INFRASTRUCTURE	Roads, sewer, water etc.	0.030	Med-4	0.12	Med-4	0.12	High-6	0.18
AFFORDABLE HOUSING	Percentage of below-market rental or for-sale housing units deemed affordable	0.040	High-6	0.24	High-6	0.24	High-6	0.24
COMMUNITY OPPOSITION	Extent of community opposition to project prior to application	0.125	Med-4	0.50	Med-4	0.50	High-6	0.75
UNCERTAINTY	Unknown factors that can arise during the development that can have a negative impact	0.100	High-6	0.60	High-6	0.60	Low-2	0.20
TOTAL		1.000		4.83		5.43		4.53

Of the various risk factors that generally confront development projects, different factors will loom larger, depending on whether the project is 1) a “big-R” redevelopment project that is located in an officially-designated redevelopment areas and has already been deemed consistent with formal municipally-adopted redevelopment plans; 2) a “little-r” redevelopment project that involves new development on a previously-developed or infill site but without any formal area designation; or 3) a “greenfield” project on previously-undeveloped land located in a rural or low-density suburban context.

While greenfield projects share some risk factors with redevelopment projects, the more significant factors affecting greenfield projects are addressed early in the development process. This allows the greenfield project to enjoy a sharp drop in its weighted risk score very early. Conversely, after addressing these same risk factors early in the process, an optimistic redevelopment scenario will still have significant risk since the remaining factors – environment, construction and uncertainty – have a greater impact on a typical redevelopment project than they do on a greenfield project.

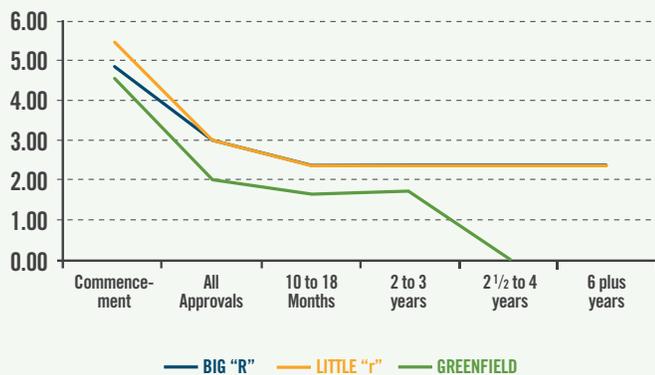
The timeline of a development project has a significant impact on risk. As shown in Figure 3, as time progresses the risk rating drops. Figure 3 displays the periodic risk ratings from Figure 1 in a line chart. The most notable changes, especially for a greenfield development, are experienced once all approvals are obtained after the project’s commencement. The greenfield rating drops by more than half once all approvals are received and it consistently maintains a much lower rating than the others.

A REDEVELOPMENT PROJECT THAT MOVES MORE QUICKLY THROUGH THE IDENTIFIED MILESTONES WILL WIND UP BEING LESS RISKY OVERALL AND WILL PROVIDE A DEVELOPER WITH MORE PREDICTABILITY, WHICH CAN BRING DOWN THE OVERALL COST OF THE PROJECT.

The most significant divergence between greenfield and redevelopment is at two to three years from commencement. At this point or even earlier, most greenfield developments are complete and the developer has minimal if any risk going forward. At this same point in time, redevelopment projects are typically only half-complete and still carry a high level of risk. There is also a significant difference in the developer’s financial position. Financial position is not visible from the graph but it is another advantage of greenfield development over redevelopment. Upon completion of a development, the developer has access to capital and is likely going to invest its capital in the next project or projects. In greenfield developments, a developer will have access to its capital earlier than in redevelopment. This benefit must be considered because it will likely have a significant impact on the developer’s overall return in a given timeframe.

It is important to note that a redevelopment project that moves more quickly through the identified milestones will wind up being less risky overall and will provide a developer with more predictability, which can bring down the overall cost of the project.

Figure 3. Risk Rating Over Time, by Type of Development / Redevelopment Project



The risk involved in any development project tends to diminish over time, but redevelopment projects start out riskier than greenfield developments and stay riskier longer.

MITIGATING COST AND RISK

In the course of the interview process, several consistent cost and risk themes were identified by participants related to redevelopment projects. It became evident that developers do want to work in redevelopment areas and they do not have an inherent bias against redevelopment. All the developers interviewed had experience in redevelopment projects, most planned to continue working in redevelopment areas and some were even expanding their business activities in redevelopment. For some developers, their openness to redevelopment was market-driven – decline in the suburban housing market and the increased demand for urban apartment markets – but for others, redevelopment has always been part of their business activities and will remain so.

Developers with significant greenfield experience were not opposed to redevelopment, but were swayed towards greenfield work primarily because of the perceived complexities and barriers, such as time constraints and financial requirements, that redevelopment presents. Redevelopment was considered a new type of business with different risk and feasibility assessments, and for those reasons these developers would only engage in it on a limited basis.

Below are some key redevelopment cost- and risk-related observations identified by the participants and expanded on in a literature review, along with recommendations on how to mitigate them.

Organized municipalities are key. An important distinction between greenfield and redevelopment projects is that the latter require more extensive interaction and collaboration with municipalities and governmental agencies. This requirement often deters developers from engaging in redevelopment projects because they may require navigating a lot of local processes that can cause frustration, delays, and financial risks.¹⁰

A municipality can attract more redevelopers by being more organized and offering a clear and streamlined process for implementing a redevelopment project, which in turn serves to reduce the overall time and increase the efficiency of the redevelopment process. Having a municipality actively

manage the process reduces delays and the community can benefit more easily and quickly from the proposed redevelopment project.

Saving time also translates into saving money. This is true for all parties involved but perhaps is most relevant to the developer. Redevelopment projects have a reputation for being time-consuming and lengthy which serves as a deterrent to some developers. Furthermore, all developments require a significant amount of capital. Developers put their own money at risk, and frequently capital from equity investors and lenders. Thus the longer it takes to complete the project, the more money the developer will pay in financing costs. The financing costs are built into the budget and can put significant pressure on the economic feasibility of the project. Therefore an organized municipality is more likely to enhance the economic feasibility of the redevelopment of its community.

A MUNICIPALITY CAN ATTRACT MORE REDEVELOPERS BY BEING MORE ORGANIZED AND OFFERING A CLEAR AND STREAMLINED PROCESS FOR IMPLEMENTING A REDEVELOPMENT PROJECT

A collaborative relationship between municipality and developer is critical. Another deterrent that developers note in their hesitation to engage in a redevelopment project is the lack of support they encounter from the municipality during the redevelopment process. A supportive municipality will need to be consistent in its vision and have a working partnership with the developer. It is important for the developer to align its goals with that of the community, but it is equally important for the municipality to be flexible and willing to work with the developer.¹¹ In some instances, market realities conflict with the municipality's redevelopment plan (for example, the plan may call for mixed-use with retail space in a market that is lacking demand for retail). Under these circumstances, it is critical

that the municipality face market realities and work with the developer to adjust the plan in order to meet current market conditions, with flexibility to make changes over time. If the municipality is not willing to modify the plan or work out an alternative with the developer, the redevelopment may never get started.

In a supportive redevelopment environment, project issues should be considered municipality issues, not just developer issues; this means it may be necessary at times for the municipality to take on issues hand-in-hand with the developer. For example, in addition to local municipalities, most redevelopment projects will involve governmental agencies from the county, region and state. These agencies are included in the process for good reason; however, in some cases they may hold up the process for impractical reasons. The agencies are often not as familiar with the project details as the municipality and they may have an agenda that conflicts with the goals of the community. To resolve this, it may become necessary for the municipality to stand in support of the developer to ensure that the project continues.¹²

Administrative capacity must come first. Capacity at the municipal level can make the difference between successful redevelopment projects and ones that never take shape. Municipalities that have dedicated resources – human, financial and consolidated authority – have a much higher success rate in redevelopment than those that do not. Resources can be dedicated to start and oversee the redevelopment process, enabling the completion of such tasks as identifying areas in need of redevelopment; early commencement of the designation and planning process; overall project facilitation; land assemblage; environmental remediation; and developer selection. If the community goes through an effective redevelopment planning process, the planning for areas in need of redevelopment is more likely to address local concerns early and the final plan will more likely be in line with the needs of the community.

Capacity and dedicated resources, both human and financial, are not available in some municipalities, particularly smaller municipalities. In this situation, there are two possible scenarios. In the first, a developer may approach the munic-

ipality with a proposal and initial plan to redevelop a specific area or parcel. In this instance, it is the developer making the case for redevelopment and taking the first steps in laying out the plans.¹³ When this happens there is an increased likelihood that the development will not be entirely successful in satisfying the needs of the community. This is because the municipality was not involved early enough in the process so that it could align the developer's goals more completely with those of the community.

IT IS CRITICAL THAT THE MUNICIPALITY FACE MARKET REALITIES AND WORK WITH THE DEVELOPER TO ADJUST THE PLAN IN ORDER TO MEET CURRENT MARKET CONDITIONS, WITH FLEXIBILITY TO MAKE CHANGES OVER TIME.

The other likely scenario is that the municipality will need to hire redevelopment consultants to assist with the planning, implementation and monitoring of the redevelopment. Consultants can be costly and these costs early in the process will need to be absorbed by the municipality. However, once the process is further along and a developer is selected, some of these costs can be shared with the developer. Most developers are flexible and are open to providing reasonable assistance as long as that assistance can be financed while maintaining the project's economic feasibility. Alternatively, the municipality could finance the initial costs by issuing debt that would be paid off with project funds; this will be discussed in detail later in this report.¹⁴

In either of these scenarios, it is important for the municipality to engage the community proactively. The best-case scenario is for the engagement strategy to concentrate on building consensus around a site's end use and the parameters for its development. In a less proactive scenario, the strategy may be simply to communicate accurately the pros and cons of a proposed development project rather than relying on the developer to make the case.¹⁵

MUNICIPALITIES THAT HAVE DEDICATED RESOURCES – HUMAN, FINANCIAL AND CONSOLIDATED AUTHORITY – HAVE A MUCH HIGHER SUCCESS RATE IN REDEVELOPMENT THAN THOSE THAT DO NOT.

Previous redevelopment experience is very beneficial. The development community has varied levels of experience in redevelopment projects, and many developers and contractors are not well versed in dealing with the unique and unpredictable challenges, such as partnering with municipalities, that are inherent in redevelopment projects. There is no such thing as a typical redevelopment project; therefore a developer and contractor must be prepared for, and capable of working through, unforeseen issues that arise. Municipalities will need to keep this in mind when they are selecting a developer for a redevelopment. A developer experienced in redevelopment and/or infill development is critical and should be part of the municipality's qualifying criteria.¹⁶

The need for experienced developers and contractors in redevelopment projects limits the number of capable people available for the job. This puts added financial pressure on a redevelopment project because this unique experience can come at a financial premium and it can be difficult to get the required expertise in the timeframe needed. Furthermore, with delays that are common in redevelopment projects, contractors may no longer be available when needed because of commitments to other jobs. This is a vicious cycle that tends to perpetuate itself in redevelopment.

Developer profit can disappear quickly. When a redevelopment project is being developed by a for-profit development firm, there has to be a profit to motivate the developer. Profits will provide the developer compensation for taking on the risk, incurring the time, investing the capital needed and providing a small cushion for unforeseen conditions.

As previously discussed, redevelopment projects can be very risky and consume a lot of time and capital. At times, it can be challenging for a developer to secure a profit commensurate with the efforts and risks, especially the inherent uncertainty in the process and the length of time involved, in a redevelopment project. After factoring in market constraints (i.e. the price that someone is willing to pay for the end product), the developer's profit can disappear quickly. Also, market conditions at the onset of the development can change before completion, especially given the time required for a redevelopment project. Furthermore, since hard and soft costs are essentially fixed,

weakening market conditions leave less and less room for the developer to be able to make adjustments in order to keep the project economically feasible.

If market conditions are weak at the beginning of the project, it will likely not get started without additional financial subsidies or cost-saving concessions. This puts the onus on the municipality. At times, when the private sector cannot provide socially valued goods profitably, the public sector must intervene to provide a solution where one would not otherwise occur.¹⁷ In these instances, municipalities (and state and county agencies) may need to offer assistance and financial incentives to get developers to work on redevelopment projects in their communities and/or to assist developers with obtaining county or state assistance.

An example of a common assistance program that municipalities have provided successfully is a payment in lieu of taxes, or a PILOT. A PILOT is a payment made to the municipality by the property owner that replaces the owner's real-estate tax obligation. This payment is an agreed-upon amount for a predetermined time period. The amount paid is usually less than what the property owner would have otherwise paid in real-estate taxes but, importantly, is fixed and predictable. A PILOT is essentially a reduction in the owner's real-estate taxes that will not fluctuate for anywhere from five to 30 years. During this time the developer can benefit directly from the PILOT by holding the property and enjoying lower municipal payments and a predictable annual cost; or indirectly, by selling the property and capitalizing on this benefit in the sales price. The municipality can derive a significant benefit from this as well. Typically, the property is vacant, abandoned or underutilized prior to redevelopment and does not generate much, if any-

thing, in tax revenue for the municipality. However, once the land is redeveloped, the PILOT will provide the municipality with more revenue than what the previous use provided in regular taxes. Once the PILOT term expires, full taxes will be paid.

IF MARKET CONDITIONS ARE WEAK AT THE BEGINNING OF THE PROJECT, IT WILL LIKELY NOT GET STARTED WITHOUT ADDITIONAL FINANCIAL SUBSIDIES OR COST-SAVING CONCESSIONS.

Furthermore, when regular real estate taxes are paid to a municipality, they are split with other government entities, such as school districts, the county and the state. By contrast, when a PILOT is paid to a municipality, up to 95 percent of the payment can stay within the municipality and does not get split with the other government entities. (The remaining 5 percent will be paid to the county.) Under this circumstance, the PILOT again may be a lower payment than a regular real-estate tax, but can result in an increase in funds collected by the municipality because of the higher percentage retention rate.¹⁸

Other forms of incentives include (but are not limited to) preferential zoning (e.g. high density zoning); incentive grants (e.g. tax incentives under the GROW NJ program) to fill gaps in financing; federal and state subsidies; and public acquisition assistance (e.g. eminent domain or municipality land acquisition).

Incentive programs could be strengthened. The above-mentioned incentives can be very helpful in providing the needed

catalyst for a developer to proceed with a redevelopment project; however, they do not come without downsides. A PILOT is often the best financial incentive a municipality can provide because taxes are one of the highest expenses for a development. Historically, PILOTs have been very successful for many redevelopment projects. Critical to the successful use of a PILOT is that the term must be significant enough to have a meaningful impact on the economics of the development. An example of this is a 30-year PILOT equivalent to a percentage of the final development's annual gross revenue. In most cases, this would be significant enough to allow adequate time for the developer to capitalize on the tax benefit and to justify financially proceeding with the development. Conversely, in redevelopment projects in areas designated "in need of rehabilitation," PILOTs may only be offered for a term of five years. Often five-year abatements do not offer enough economic impact on their own to make projects in emerging markets viable. In such instances, it may be necessary for municipalities to stack incentives by offering a five-year PILOT coupled with preferential zoning and/or state tax breaks or subsidies. To attract the right developer, the municipality must make it financially worthwhile for the developer to take on the project.¹⁹

Many state and federal subsidies come with a "prevailing wage" clause that requires paying union-negotiated labor rates that are higher than typical market labor rates. In many cases the subsidy does not compensate for the higher labor costs, making the programs useful in fewer situations. Depending on the scale and construction type of the redevelopment project, the developer may employ prevailing-wage labor to secure the needed skill set or abide by specific local or political circumstances. This will allow the developer to take advantage of state or federal subsidies to cover some of the costs of the development and to assist in making the project economically feasible.

CONCLUSION

New Jersey is the most developed state in the nation, and it is still growing. In order for this growth to continue while allowing natural areas and farms to be preserved, future development will need to take place on previously developed sites. This means that redevelopment and infill development are the future of growth in the state of New Jersey. For this to happen, some obstacles to redevelopment will need to be overcome.

Greenfield development has been the default model for the state's growth over the last 60 years and has transformed many suburban and rural towns. Developers now have decades of experience doing this type of development, and are adept at making the process more predictable and therefore less risky. These lower risks also generally make a greenfield project relatively less expensive than a redevelopment project of similar size, since redevelopment usually involves greater

MANY OF THE RISK FACTORS THAT DISTINGUISH REDEVELOPMENT PROJECTS FROM GREENFIELD PROJECTS ARE AT LEAST PARTIALLY UNDER THE CONTROL OF THE HOST MUNICIPALITIES.

complexity, thanks to factors like land assembly, a mix of land uses in the project, more expensive construction techniques, and/or a higher probability of a requirement for environmental remediation.

But while redevelopment is often more expensive than greenfield development on a per square foot basis, it does offer significant short- and long-term public benefits, such as relieving development pressure on open space, reducing per-unit infrastructure costs and increasing potential users of and therefore the viability of a public transportation system. Conversely, greenfield development may cost less in the short run but cost the public more in the long run, for things such as maintenance of new roads and infrastructure and the cost to provide extended public services. This is especially true if the development is low-density development, which raises per-capita costs. These additional costs are not built in to the initial development pro forma, but rather are borne by the community in subsequent years.

For New Jersey to reap the benefits of redevelopment, the process needs to become easier. Based on interviews with developers and analysis of specific projects, it is apparent that redevelopments can be profitable and that there is willingness on the part of the development community to build such projects. However, a successful redevelopment project will require more than just a willing developer and an economically feasible development. Committed and cooperative municipal leaders can play a significant role in mitigating risks.

Many of the risk factors that distinguish redevelopment projects from greenfield projects are at least partially under the control of the host municipalities. Municipal leaders can speed the process by officially declar-

ing an “area in need of redevelopment” or an “area in need of rehabilitation” and making needed zoning changes ahead of time. They can accelerate land assembly by acquiring individual parcels as opportunities arise. They can anticipate and minimize community opposition by conducting effective public outreach about a project, or even by engaging citizens in discussion about the need to declare an area in need of redevelopment or rehabilitation before a developer is secured. They can streamline the permitting process for redevelopments. There are also a number of tools and incentives at the state level that municipalities can help developers secure that can assist in promoting redevelopment. All of these activities require municipalities to have or hire the capacity to manage and shepherd a multi-year process.

In general, to ensure that its community is not left behind, a municipality needs to take a proactive approach towards the issues facing redevelopment. This includes understanding the long-term vision for the town as well as the realistic market opportunities. An economic and land use assessment, coupled with strong community engagement, is a good starting point.

Lastly, municipalities must be flexible. In real estate development, especially in redevelopment, multiple changes and revisions to a plan are to be expected. Most of these changes are caused by factors that are out of the control of both the developer and the municipality. A common example is changes in market conditions. Such changes can require that the parties involved go back to the drawing board for a complete restructuring of the project. Municipalities should be aware of this and keep an open mind. They should think of developers as partners and leverage their knowledge and experience. A municipal leader must focus on what is best for the community: A successful redevelopment that didn’t turn out exactly as originally planned is still preferable to a failed redevelopment.

Redevelopments can be successful in revitalizing a community, as has already been demonstrated in many communities throughout New Jersey. As the state continues to grow, redevelopment will continue to be a great opportunity for many communities to redefine and recreate previously developed sites. The key to capitalizing on these opportunities will reside with the local municipality.

ENDNOTES

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ACKNOWLEDGEMENTS

This report was made possible by the participation of developers, researchers, reviewers, New Jersey Future staff and New Jersey Future supporters.

Thanks to all of the following participating developers for their efforts and time, and for giving the author unprecedented access to development details:

- » **Dave Fisher** *vice president of governmental affairs, K. Hovnanian Homes*
- » **Steve Santola** *executive vice president and general counsel, Woodmont Properties*
- » **George Vallone** *president, Hoboken Brownstone Company*
- » **Tim Henkel** *senior vice president, Pennrose Properties*
- » **Jason Kaplan** *president, Kaplan Companies*
- » **Peter Porraro Sr.** *executive managing director, Mill Creek Residential Trust*

Special thanks to George Vallone of Hoboken Brownstone Company for assisting in the development of materials used in the project and for gathering the support of fellow developers.

Thank you to the following reviewers for taking the time to read the report and provide detailed feedback: George Vallone, Peter Porraro and Peter Reinhart, director of the Kislak Real Estate Institute at Monmouth University, with special thanks to Peter Reinhart whose direction, guidance and support throughout the project were indispensable.

Thank you to the financial supporters of New Jersey Future. Their continued support has made it possible for New Jersey Future to bring together concerned citizens and leaders to promote responsible land-use policies. Such efforts support original research and analysis, such as this report.

Thank you to New Jersey Future's staff and especially to Tim Evans, Teri Jover and Peter Kasabach. Peter's support and involvement was consistent throughout this project and was essential to getting this off the ground and across the finish line.

Thank you to all of the other participants who assisted in some capacity with producing this report, here with a special mention to: Jeff Kolakowski, vice-president, New Jersey Builders Association, George Carfagno, principal at GJC Associates and Charles Tint, vice president at Premier Development.

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