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DEVELOPMENT EXACTIONS: WHAT ARE THEY?

For a number of years the term "exaction" has been used to refer to a range of requirements that cause a developer to contribute to the cost of providing the public facilities required by new development. A definition of a development exaction adopted by the North Carolina courts is as follows:

> **Exaction**. A condition of development permission that requires a public facility or improvement to be provided at the developer's expense.

When properly applied, developer exactions are legally authorized commonly used regulatory tools that can be used to ensure that a new development project "pays its own way."

Exactions and Land Subdivision

From a historical perspective developer exactions have long been associated with the approval and development of land subdivisions. Particularly in urban settings subdividers have been expected to furnish the streets and water supply and wastewater disposal systems need to serve the purchasers of lots. Most subdivision activity involves single-family residential lots; thus the burden of development exactions has tended to fall on residential developers and builders and indirectly on home purchasers. More recently, though, certain public facility costs associated with multi-family residential and non-residential development have been assigned to developers of these kinds of projects as well.

Government's Regulatory vs. Contracting Power

Developer exactions derive from government's regulatory power. In this regard they may rightly be viewed as obligatory measures that are involuntary as far as the property owner/developer is concerned. If the property owner/developer chooses to pursue even a moderately complex form of development, a local government may be in a position to require one type of contribution to infrastructure or another. Of course, there may be circumstances in which a property owner/developer believes that it is in its own best interest to contribute to or to provide public improvements to enhance the marketability of a project. A property owner/developer may voluntarily participate in arrangements for providing public improvements. In such cases what the developer contributes may be part of an effort to induce a local government to use its discretion to rezone property (see more about conditional zoning below). Or it may be part of a more formal contract in which a private party and a public agency agree to share responsibilities for constructing public improvements in connection with a private development project. In concept these voluntary contractual and quasi-contractual

arrangements may be contrasted with classic development exactions imposed under the government's police power. From the standpoint of both the developer and the governmental unit there is sometimes a blurry line between involuntary and voluntary means of financing public infrastructure and between the regulatory and public contracting powers of government.

In-Kind Exactions vs. Monetary Exactions

Another key distinction among development exactions is between "in-kind" exactions and monetary exactions. Certain kinds of traditional exactions are classified as "in-kind" since the landowner/developer provides the property directly. "In-kind exactions" may involve requirements that a developer help to provide public facilities by either dedicating (donating) land or an interest in land to a governmental unit for a public use. Or they may involve requirements that the developer construct or install public improvements such as paved streets or recreational improvements in areas that have been publicly dedicated. In addition, the land and improvements that developers are expected to provide are ordinarily located "on-site" (within or on the perimeter of project boundaries). "On-site" facilities such as these can more easily meet the constitutional test that requires exactions to principally serve the residents or users of the development.

Monetary exactions are attractive to local governments for two reasons. First, the use of fees to divide and apportion the costs of public facilities made necessary by new development promises to make exactions more equitable, fair, and uniform. Second, some exaction fees allow local governments to assign to the developer some of the costs of providing certain facilities benefiting a wider service area that cannot legally be assigned to developers using traditional "in-kind" exactions. For example, a developer might be required to pay a fee covering a prorated portion of the cost of constructing a sewage pump station serving new development on one side of town even though the developer could not legally be required to construct the lift station without contribution from other parties.

One type of monetary exaction authorized in North Carolina is the collection of a fee in lieu of some sort of dedication or construction requirement. Instead of expecting a dedication of land, a local government may be authorized to accept a money payment instead. A fee-in-lieu represents the value of the land that would otherwise have been dedicated or the value of the improvement that otherwise would have been provided. Cities and counties are authorized under their subdivision authority to accept fees in lieu of accepting the dedication of recreation land. In addition cities are allowed to accept fees from subdividers as an alternative to requiring them to make road improvements.

The other major type of monetary exaction is the impact fee. The North Carolina General Assembly has not adopted general enabling legislation for either cities or counties to adopt impact fee ordinances. It has, however, authorized such ordinances for particular cities and counties in a series of local acts. Several dozen North Carolina

cities and counties have been authorized to use such fees in one form or another to help fund various types of public facilities.

Impact fees represent a systematic, comprehensive way of funding the new capital facilities required by new development. Impact fees may be used to fund a wide range of public facilities associated with development infrastructure, including water and sewerage systems, parks and open space, and stormwater control facilities. Impact fees, also known as facility fees or project fees, are intended to fund facilities serving entire areas or regions of a jurisdiction, facilities that are "off-site" with respect to the development for which the fees are paid. For example, an impact fee might be collected from a developer to help fund a large stormwater detention facility some distance from the project. In addition, impact fees can be applied to apartment, condominium, commercial, and even office and industrial developments.

General authority for local governments to employ impact fees is very limited. The North Carolina Supreme Court has held that counties lack authority to impose impact fees to help finance public school facilities. Durham County Land Owners Assn. v. County of Durham, 177 N.C. App. 629, 630 S.E. 200, *rev. denied*, 360 N.C. 532 (2006). However, a local government that supplies water or furnishes wastewater disposal as a public enterprise may incorporate into its fee structure a component that is designed to allow the recovery of a pro-rated portion of expanding the water supply or sewage collection/treatment system to accommodate new growth. Town of Spring Hope v. Bissette, 53 N.C. App. 210, 280 S.E. 490 (1981), *aff'd*, 305 N.C. 248 (1982). Such a capital expansion fee can function much like an impact fee. See G.S. 160A- 314(a).

In summary, then, development exactions typically fall into one of four categories: (1) requirements that land be dedicated to the public for streets, parks, utility easements, and the like; (2) requirements that facilities or improvements be constructed or installed on land or within easements so dedicated; (3) requirements that fees be paid in lieu of compliance with dedication or improvement requirements; and (4) requirements that developers pay impact fee or facility fees that reflect their respective prorated shares of the costs of providing new roads, utility systems, parks, and other public facilities serving the entire area. In a more abbreviated way these forms of exactions can be summarized as follows: (1) land dedication; (2) infrastructural improvements; (3) fees-in-lieu; and (4) impact fees. Not all of these forms of exactions are authorized in North Carolina, nor are all forms of exactions available for all types of facilities.

EXACTIONS AND THE LAW

Enabling Authority for Exactions

Any North Carolina local government that imposes exactions must be prepared to demonstrate that the exactions are based on state legislative authority allowing them to be used. It is generally understood that reasonably specific enabling authority is essential to the validity of any form of exaction. Unless they are based upon such

statutory language, exactions are vulnerable to a claim that they are beyond the scope of government's legal authority or that they are unauthorized taxes.

Constitutional Issues

In North Carolina, as in most states, the statutes affecting exactions establish the form an exaction may take and the purpose or type of public facility for which an exaction may be used. What they sometimes do not address is the scope or extent of an exaction requirement that may be imposed upon a developer. In such an instance whether an exaction is a legitimate one or amounts to an abuse of power is generally viewed as a constitutional issue. The constitutional aspects of exactions thus attract a good deal of attention. Unless exactions are flexibly applied, they may amount to an unconstitutional taking of private property for public use without just compensation or, less likely, a denial of the property owner's due-process rights. For example, a requirement that a subdivider build an arterial street along the subdivision's boundaries or dedicate land for a park that serves an area substantially larger than the development might be vulnerable to such a claim.

In Nollan v. California Coastal Comm'n, 483 U.S. 825 (1987), the U.S. Supreme Court ruled that an "essential nexus" or connection must exist between the purpose of a development exaction and some problem or need generated by the particular development in question. Several years later, the same court in Dolan v. City of Tigard, 512 U.S. 687 (1993), extended this principle by ruling that the amount or extent of the exaction imposed must represent only the developer's fair share portion of the problem so addressed. According to *Dolan*, the U.S. Constitution requires "rough proportionality" between the impact of the development on the need for public improvements and the nature and extent of the exaction. Although precise mathematical calculation is not required, some sort of individualized determination must be made to justify an exaction requirement in a particular case. The Court also held that a local government bears the burden of proving that an exaction is constitutional.

These cases, especially *Dolan*, served to complement the "rational nexus" test announced by the North Carolina Court of Appeals some years earlier in Batch v. Town of Chapel Hill, 59 N.C. App. 692, 297 S.E.2d 632 (1982), *cert. denied and appeal dismissed*, 307 N.C. (1983). The *Batch* test asks whether the exaction has a rational nexus to the nature and impact of the development proposed. The test embodies two principals: (1) the attribution principle and (2) the proportionality principle.

In determining whether an adequate connection exists, it first must be shown that the development will create a need for new capital facilities, the so-called "attribution" principle. A local government need not prove that exaction requirements were assessed to meet a need solely generated by a particular project. Instead, an adequate nexus is sufficiently established if the local government can demonstrate that a series of developments have generated a need to provide public facilities for the growth that occurs.

The second principle, the proportionality principle, requires that a "subdivider can be required 'to bear that portion of the costs which bears a rational nexus to the needs created by, and benefits conferred upon the subdivision.'"

The proportionality principle first applies to the developer's share of the costs. The principle implies that the developer may be expected to shoulder no more than the proportionate share of the costs of new facilities that can be attributed to the new project. A corollary of this principle is that new development may not be assigned the costs of bringing substandard facilities serving the existing population up to the service level standards that apply to new facilities. The public facilities and improvements provided by or funded by the developer must provide sufficient benefit to the development for which the exaction was imposed.

The recent U.S. Supreme Court case of Koontz v. St. Johns River Water Management District, 570 U.S. ____ (2013), provides further guidance. According to *Koontz*, the *Dolan* test applies not only to demands for property that are attached to approved permits. It also applies to demands for property that an applicant refuses to accept. A governmental agency may deny a development approval if it has the discretion to do so. But what it may not do is to withhold a permit or approval because an applicant refuses to accept an unconstitutional condition. The court in *Koontz* leaves open the question of how one determines when the discussion of mitigation alternatives becomes a demand for property. In addition, *Koontz* did clarify that the *Dolan* test applies to both monetary exactions as well as "in-kind" exactions of property.

DEVELOPMENT PERMISSIONS ASSOCIATED WITH EXACTIONS

Driveway Permits

One less well-known form of development exaction comes in the form of conditions attached to driveway permits. These permits are issued by cities inside their city limits and by the North Carolina Department of Transportation with respect to certain state roads and highways. (Counties have no comparable power.) G.S. 160A-307 allows a city to adopt an ordinance regulating the size, location, direction of traffic flow, and manner of construction of the driveway connections into its streets. Driveway permits are most important when the project being served is a large non-residential development that disgorges substantial traffic onto adjacent streets or highways that are already near capacity. In association with driveway connections a city may require the construction (or reimbursement of the cost of construction) and public dedication of medians, acceleration and deceleration lanes, and traffic storage lanes. The statute allows these exactions only if (1) the need for the improvements is reasonably attributable to the traffic using the driveway, and (2) the improvements serve the traffic of the driveway. These last two requirements are designed to ensure that the exaction meets the constitutional tests described above.

NCDOT enjoys similar authority with respect to the state highway system. The department may require essentially the same kinds of traffic-related road

improvements and right-of-way dedication with respect to driveways on state highways with over 4,000 vehicle trips per day (G.S. 136-18(29)). One important application of this authority concerns driveways serving public and private schools. Upon acquiring land for a new school or prior to beginning construction of a new school or expanding an existing school, the school sponsor is directed by G.S. 136-18(29a) to request an evaluation and recommendation from NCDOT. The written evaluation and recommendation is intended to ensure that school driveway access points comply with NCDOT driveway access standards. School entities need not necessarily comply with all the recommendations that NCDOT may have, but NCDOT is nonetheless authorized to require highway improvements that are necessary for safe state highway ingress and egress.

Subdivision Plat Approval

Development exactions have long been associated with subdivision approval. The first type of exaction authorized by the General Assembly was the dedication of land for street rights-of-way and easements for utility purposes. In 1955 cities were authorized to require the dedication of land for these purposes as a condition of subdivision plat approval. Parallel authorization was adopted for counties four years later.

In 1961 cities gained the power to require developers to construct roads and provide and install utility lines within the dedicated easements and rights-of-way. Comparable authority was provided to counties in 1973. North Carolina's land subdivision control enabling legislation includes language adopted in 1961 (cities) and 1973 (counties) that authorizes local governments to require the construction of "community service facilities." This terminology has been understood to include road improvements, recreation facilities, and a range of utility facilities and improvements needed to serve the local needs of a subdivision. G.S. 160A-372(c) also allows cities to collect fees in lieu of construction of street improvements. The funds may be used for “the development of roads, including design, land acquisition, and construction.” The money may be used for roads serving more than a single subdivision or development. This authority is particularly important in light of Buckland v. Town of Haw River, 141 N.C. App. 460, 541 S.E.2d 497 (2000), which held (perhaps wrongly) that a municipality has no authority to require a subdivider to pave and install curb and gutter on streets abutting the subdivision.

In 1971 land dedication requirements were authorized for another purpose. In that year cities were first allowed to require subdividers to dedicate land for use as a recreation area (G.S. 160A-372(c)). Counties were provided similar enabling authority two years later (G.S. 153A-331(c). Counties were authorized to allow the payment of fees in lieu of dedication of recreational land in 1975. Municipalities were granted similar authority in 1985.

Zoning Decisions

Historically if the development of land did not involve the subdivision of land and was subject only to zoning regulations, local governments have lacked legal authority to require the developer to provide new public facilities, even if they were needed to serve the new development. Today there continues to be no express authorization for exactions imposed for uses "permitted by right," even if those uses may be subject to a site-plan review procedure. Likewise there is no authorization for a local government to impose an exaction as a formal condition imposed upon a conventional rezoning to a general-use zoning district.

Many types of large-scale development (e.g., apartment complexes, shopping centers) create the need for new infrastructure to an extent comparable with that of a large residential subdivision, but have been outside the scope of the subdivision exaction statutes. The North Carolina General Assembly provided the first authority to use exactions in the context of zoning in 1971. In that year zoning legislation was adopted that provided that certain requirements could be added as conditions to the granting of a special-use or conditional-use permit. The language, which remains intact today for cities in G.S. 160A-381(c), provides in part as follows:

> . . .
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> The (zoning) regulations may also provide that the board of adjustment or city council may issue special use permits or conditional use permits in the classes of cases or situations and in accordance with the principles, conditions, safeguards, and procedures specified therein and may impose reasonable and appropriate conditions and safeguards upon these permits.
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> . . .
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> Where appropriate, such conditions may include requirements that street and utility rights-of-way be dedicated to the public and that provision be made of recreational space and facilities.
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> . . . (Underlining added.)

(Similar but slightly different language in G.S. 153A-340(c1) provides comparable authorization for counties.) G.S. 160A-381 (c) clearly allows cities to require the dedication of land for public streets and utility easements. It likely also permits requirements for the dedication of land for recreational space, the construction of recreational facilities, and the improvement of recreational lands so dedicated. In addition, it is possible, though less likely, that a court might construe the power to add "reasonable and appropriate conditions" to a conditional-use or special-use permit to include the power to impose other types of exactions that are not specifically listed.

In the 2001 case of Massey v. City of Charlotte, 145 N.C. App. 345, 550 S.E.2d 838 (2001*), cert. denied*, 354 N.C. 219 (2001), a North Carolina appellate court first upheld

the use of conditional zoning. That technique involves rezoning land to a conditional zoning district based on an approved site plan. Site-specific development conditions may be attached to the rezoning ordinance itself; no conditional-use permit or special-use permit need be involved. However, the terms and conditions of the rezoning must be approved both by the local government and the petitioner. It is not uncommon for a petitioner/developer to agree to provide certain public facilities at its own expense as part of the inducement for a local government to rezone. The statutory language that expressly recognizes conditional zoning, adopted in 2005 in G.S. 160A-382(b) and G.S. 153A-342(b) provides that:

> Conditions and site-specific standards imposed in a conditional district shall be limited to those that address the conformance of the development and use of the site to city ordinances and an officially adopted comprehensive or other plan and those that address the impacts reasonably expected to be generated by the development or use of the site.

The phrase referring to development conditions that "address the impacts reasonably expected to be generated . . ." may be viewed as a limitation on the scope of the contributions to which a petitioner may be expected to agree when property is proposed for rezoning to a conditional district.

RELATED FORMS OF PROPERTY OWNER PARTICIPATION

Development Agreements

Another medium for property owner contributions for the construction of public facilities and improvements is through formal development agreements. See G.S. 160A-400.20 to -400.32. This authority allows local governments and property developers to enter into long-term agreements concerning development projects of at least 25 acres. A local government and a developer may share the responsibility for financing new public facilities that will serve new growth. One limitation on a local government's power in this regard is reflected in G.S. 160A-400.20(b). It provides in part that when entering into such agreements, "a local government may not exercise any authority or make any commitment not authorized by general or local act and may not impose any tax or fee not authorized by otherwise applicable law." Apparently the authority to enter into a development agreement does not necessarily expand a local government's power to induce developer contributions for public infrastructure.

Ad Hoc Infrastructure Agreements

Local governments and developers may also enter into certain agreements concerning specific infrastructure. In some cases it may be desirable for a developer to construct facilities and improvements that serve more than just the developer's own property. Local governments may offer to reimburse the developer (or his contractor) to the extent that the improvements are "oversized," and a local government may not insist upon these arrangements through regulation. G.S. 160A-499 and G.S. 153A-451 apply

to the construction of local government infrastructure anywhere within a local government's planning jurisdiction. The new law authorizes reimbursement agreements with developers and property owners for a wide variety of purposes, including water and sewer utilities and street and traffic control improvements. In order to qualify, the facility or improvement must be included on the local unit's capital improvement plan. An alternative model for public enterprise improvements that are adjacent or ancillary to a private land development project is provided by G.S. 160A-320 and G.S. 153A-280. They allow a city or county to reimburse those costs associated with the design and construction of improvements that are in addition to those required by local land development regulations. A third line of authority in G.S. 160A-309 allows cities to enter into reimbursement agreements for intersection and roadway improvements that lie within city limits. A fourth source of authority allows NCDOT pursuant to G.S. 136 -18 to enter into agreements with developers seeking driveway permits who are willing to construct "oversized" road improvements.

Adequate Public Facilities Provisions

It is also useful to compare development exactions with "adequate-public-facilities" (APF) programs. Adequate public facilities programs are based on the notion that growth should be directed into areas that enjoy excess public facility capacity or that will be served by public facilities concurrently with the build-out and occupancy of the development. If a development proposal will overburden existing facilities, then APF programs generally provide a series of alternatives. The developer may postpone or phase the development until the facilities are provided by government. The developer may redesign the development to reduce the impact on public facility capacity. However, some jurisdictions make it clear that a developer is invited either to "mitigate" the public facility deficiency by paying a fee to the local government that it may use to expand or construct the necessary facilities or improvement, or the developer may install or construct the facilities directly.

In two recent appellate cases, however, North Carolina courts have struck down public-school APF programs in which a "voluntary mitigation fee" was a central feature of the program. In Union Land Owners Assn. v. County of Union, 201 N.C. App. 374, 689 S.E.2d 504 (2009), rev. *denied*, 364 N.C. 442 (2010), the Court of Appeals invalidated Union County's program on grounds that the ordinance was not based on appropriate state enabling authority in either the zoning or land subdivision statutes. The court noted that Union County had sought but failed to obtain local legislation authorizing school impact fees. More recently, in Lanvale Properties, L.L.C. v. County of Cabarrus, 366 N.C. 142, 731 S.E.2d 800 (2012), the North Carolina Supreme Court ruled invalid a Cabarrus County program with similar features for some of the same reasons. In each case the county established a schedule of fees for developers to pay to mitigate facility deficiencies. As a result of these two cases, it remains to be seen whether a local government may by ordinance set forth measures other than fees that developers may use to mitigate development impacts on inadequate public facilities, instead of simply being denied development permission altogether.

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