



RETHINKING REVENUE

PUTTING PUBLIC ASSETS TO WORK

→ Examining the Potential of Urban Wealth Funds for North American Cities



ABOUT THE AUTHORS

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He is the author of 'The Public Wealth of Nations,' *The Economist* and *Financial Times*'s best book of the year, as well as 'The Public Wealth of Cities' and writes regularly in international media.

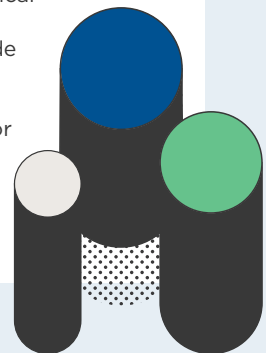
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ABOUT GFOA

The Government Finance Officers Association (GFOA) represents over 21,000 public finance officers throughout the United States and Canada. GFOA's mission is to advance excellence in government finance. GFOA views its role as a resource, educator, facilitator, and advocate for both its members and the governments they serve and provides best practice guidance, leadership, professional development, resources and tools, networking opportunities, award programs, and advisory services.

ABOUT THE RETHINKING REVENUE PROJECT

Local government revenues must adequately fund the public services that a community desires without creating excessive inefficiencies or unfairness in the revenue raising system. However, local government revenue structures are largely based on assumptions that no longer hold today due to digitization, globalization, demography, political changes, and other trends. Furthermore, fairness is becoming an increasingly important concern for public finance. It follows that this concern should include how revenues are raised. For these reasons, the Rethinking Revenue project is taking a fresh look at how revenues are raised. The project will raise new and interesting ideas like those featured in this paper and will produce guidance for state and local policy makers on how to local government revenue systems can be modernized. We hope the ideas presented in this paper will spur conversation about the possibilities for rethinking revenue.





Based on an independent valuation of the City of Boston's publicly held real estate, using a UWF could be a major source of revenue for the City.¹

What is an Urban Wealth Fund (UWF)?

Local governments are sitting on a virtual “gold mine” without realizing it. Just as a private individual or a corporation uses assets (like machines or buildings) to generate income, governments can generate income from their assets. UWFs are assigned government assets with commercial value under unified, professional management and manage them for the betterment of the local community. Examples of assets with commercial value include, but are not limited to, land, underutilized facilities, utilities, and transportation infrastructure.* Better management of these assets reduces reliance on taxes for infrastructure investment because returns from the UWF can be used to support investment instead.

What are the key features of a UWF that would distinguish it from other methods governments might use to manage assets?

- ➔ **Transparency.** All assets are clearly identified and the money they could generate in a market environment (their “market value”) is known. Many governments don’t have a centralized repository to track all of the assets they own. If they do know, they may not have visibility on the value of those assets. For example, most assets are reported at the historical acquisition cost in accordance with generally accepted accounting principles for state and local governments (GAAP). However, historical cost is not a good indicator of their current worth. It is critical to understand that market value is important **not** just for selling assets but for understanding their true worth—and to make sure they are maintained in an economically sustainable way. A fair market value also helps governments understand their income-generating potential (in ways other than sale, such as renting space to others).
- ➔ **Political independence.** Consolidating the assets with a commercial value in a portfolio within a proper governance structure will help reduce fiscal risk and delegate financial responsibility and accountability to an independent institution. The difficulties some local governments have with funding critical infrastructure or raising adequate revenues demonstrates that new approaches could be valuable. An independent holding company at arm’s length from short-term political influence will allow a government to focus on the wider economic issues by delegating the management of the commercial portfolio to a professional management team.
- ➔ **Clear objective of value maximization.** A UWF should have a comprehensive business plan that shows the link between the budget and balance sheet—a balance sheet that demonstrates to stakeholders the value of all assets (as well as its liabilities). By focusing on the fair value of assets, as well as on their full maintenance and operating costs, it is possible to identify proposals that would have positive effects on the financial wellbeing of the community.

¹ Dag Detter and Stefan Fölster, “Unlocking Public Wealth.” *Finance & Development*. March 2018.

* UWFs usually exclude parks and buildings with historical value, as these assets have important non-monetary value.

What cities offer the best example of UWFs in action?

UWFs have been used by many cities globally but not in the United States (U.S.). Copenhagen in Denmark and Hamburg in Germany are two examples with particular relevance. These cities used UWFs to create enough public resources to redevelop derelict areas inside the urban areas into attractive residential and commercial areas. Hong Kong and Singapore, in Asia, also are interesting examples but are less understood in North America.²

What is the potential benefit of a UWF?

The benefits of a UWF depend on the number and value of assets included in the fund. There is a lot of potential in U.S. cities since local governments have vast portfolios of assets with commercial possibility. Let's illustrate with a simple example. Imagine a city government operates a parking lot of with 50 spaces in the middle of the city. An UWF could develop this into mixed used building with a garage in the basement. This could not only add more parking spaces, but also add revenue from office and apartment rentals.

The Hamburg UWF is focused on redeveloping the city's harbor district into a new part of the city. Large investments have been made that created 12,000 new residential units and 45,000 workspaces, as well as a state-of-the-art concert hall and 12 new educational facilities, from kindergartens to universities—without using taxes. Copenhagen developed an even larger area and created some 33,000 new homes and 100,000 new workspaces, as well as a university for some 20,000 students. Copenhagen generated a surplus that helped fund the extension of the subway.

Hong Kong used its UWF to pay for the construction of its subway system, which is the size of NYC's subway, without using a single tax dollar. The Hong Kong train system also has remarkably affordable fares without any tax subsidy. A big part of the train system's income is derived from the housing and commercial activities that the UWF has built up around the transportation hubs of the system. This is because the land around the hubs becomes more valuable. The UWF owns some of this land and can realize the increase in value created by transit infrastructure.

For Singapore, the UWF was an essential part of taking that city from a developing economy to a developed economy in one generation. At the time of its independence, some 50 years ago, Singapore was left without food, electricity, or industry to sustain itself. With the money from the UWF, it has not only developed its economy but also supplied public and affordable housing to 85% of its population.

² This is because these cities have a very different relationship to the national government than US cities.

We have looked at cities all over the country. **When you do the math, it is easy to see that urban areas all over the United States are sitting on a “gold mine” of resources—their real estate—that is not used as efficiently as it could be.**

If professionally managed, these assets could be a great supplement to tax revenues. Every city in America has much more value hidden in the real estate portfolio than what is visible on the financial statement. There is not a day when we are not able to surprise the city management with hidden resources they have right in front of their eyes.

View from Urban Planning Consultant Joe Minicozzi



How big does a local government need to be to benefit from an UWF?

The minimum size of a fund depends on it obtaining the critical mass necessary to A) support professional management of the fund; and B) cover yield needed for other investments. That said, an UWF can apply to a single development, like a riverside/port or like a rail station. It can also apply to a large geographical area. Later in this paper we will show how Salt Lake County, Utah, analyzed all public assets within the county's boundaries, including those owned by other local governments. Potentially, smaller jurisdictions could include their assets in a UWF with other governments and get a share of the return.

How does a UWF generate revenue?

UWFs generate revenue by employing techniques that are common in the private sector. This would include developing real estate assets such as parking lots and other vacant lots, former industrial areas, or any building that could be used for better and higher use. By using techniques that a private sector developer would, a professional UWF could develop such assets into residential buildings, offices, schools, and mixed-use communities. Through a mix of tenants, the UWF would generate a diversified revenue stream that could be used to invest in the maintenance of the water system or airport, as an example. Such a comprehensive approach would not only improve the quality of services from publicly owned utilities and transportation systems but also create a more sustainable environment for the benefit of society. A government is not set up to manage commercial risk. But a UWF would be able to use the tools that aren't normally available to local governments and capture the benefit to society instead of giving it to the private sector. For example, a UWF can hire and compensate professional property managers to be competitive with private sector firms.

How is a UWF different from privatization?

UWFs are different from privatization because ownership of assets is not transferred to the private sector, and the revenue generated by the assets is reinvested back into the community. To illustrate, imagine a local government with excess property. Privatization would mean selling the property to a private interest or agreeing to a long-term lease that transfers control of the asset and revenue potential to the private sector. Using this arrangement, there have been cases where properties have been sold at prices far below market value because governments don't account for the market value of their properties—and because property sales often take place under desperate circumstances. There are countless examples, such as the Chicago parking meters to toll roads and outright sale of real estate. The professional managers of a UWF would have the skill to develop the asset to a better use with a higher value and yield.

Can UWFs be used to support the general operations of local government?

Yes, but there are advantages to first using it to invest UWF proceeds into infrastructure. Professionally managed, the wealth of a UWF would grow to the benefit of future generations and help address the difficulty may local governments face in providing the quantity or quality of infrastructure required by their communities. For example, the yield from real estate can be used to pay for the investments needed to upgrade the water system or build affordable housing and a new school.

UWF proceeds could be invested back into the community by paying for necessary infrastructure upgrades, like improving the water system.



There are advantages to using UWF proceeds to invest in infrastructure first.

Why haven't U.S. cities employed UWFs yet?

There are several reasons why UWFs have not appeared in the U.S. yet, but none of them is an insurmountable barrier. Some of the most important reasons include:

- ➔ UWFs require a different perspective on government assets not commonly taken in the U.S. In the U.S., public officials have typically considered either a traditional public ownership model or privatization. A UWF is a different approach where the assets are owned by the government but with a professional management team in place, using private sector techniques. It is separated from politics by a “holding company” at an arm’s length distance to ensure a comprehensive commercial mindset of all assets within the portfolio.
- ➔ Ownership of public assets is often fragmented between government agencies. There are transportation, utility, buildings, and land assets spread across many agencies. Using a UWF as a “holding company” with a common view of all assets (and their fair values and costs) and all the tools of professional asset management developed in the private sector to manage and develop these publicly owned commercial assets can benefit the whole community.
- ➔ In most cases, these assets may not be reported at fair market value in GAAP financial statements. If the asset, such as land, was acquired a long time ago, the historical cost may bear little relation to its fair market value. This will radically undervalue assets, especially in urban areas where space is at a premium. Most assets have been acquired for a pittance, decades or even centuries back. Low values or often no value at all attached to an asset will not incentivize investments, maintenance, or even professional management. What is not measured does not count, as they say. For example, there have been cases where local governments have operated garages or vehicle yards on waterfront property because these facilities were built when the land was worth much less (when urban cores were unattractive to potential residents). A UWF accounting for assets at their fair market value and a professional management team held accountable to develop the assets would recognize this and develop the waterfront location to be more useful and lucrative to the benefit of everybody.



Copenhagen's City and Port development serves as a model of the possibilities UWFs could unlock for U.S. cities.

What are the main opportunities for U.S. cities?

By far, the biggest asset segment is real estate, the value of which is several times that of all other assets. Excluding public parks and historical heritage sites, these government-owned real estate assets account for more than half the total value of the real estate market in most U.S. cities. But governments often know about only a fraction of these properties, most of which are not visible on government accounts. This is because local government financial and decision-making systems have not had the proper time or incentives to track these properties closely. Also, ownership of these properties might be fragmented between different departments or units of government and an UWF consolidates decision-making with purpose of generating returns for the organization. Independent valuations by Urban3 (an urban planning consultancy) of several large- and medium-sized U.S. cities showed that the market value of the public assets was many times the value stated in the government financial accounts—the so-called “book value.”

The market value was, in at least one case, as much as 70 times book value.³ In the next section, you can see a case study of Salt Lake County and some of the opportunities the County discovered.

Operational assets, such as utilities and transportation (ports, trains, buses), offer opportunities as well. They are critical for our society and our well-being. If professionally managed inside a UWF, these assets would prosper with proper maintenance and appropriate investments, and they would be used to benefit the community (including keeping user prices affordable). The big advantage of a UWF over the traditional model of public management is to insulate professional management from short-term political expediencies. Also, the revenues generated from the land portion of the UWF portfolio can be used to pay for capital asset maintenance and replacement for public utilities. This is the approach of the Copenhagen and Hamburg UWFs.

³ Evaluation performed by the consulting firm Urban3. An example of this type of analysis is available in “Unlocking Public Wealth” in the March 2018 issue of *Finance & Development* magazine. You may also consult “The Public Wealth of Cities: How to Turn Around Cities Fortunes by Unlocking Public Assets”, a March 2018 report published by Citi.

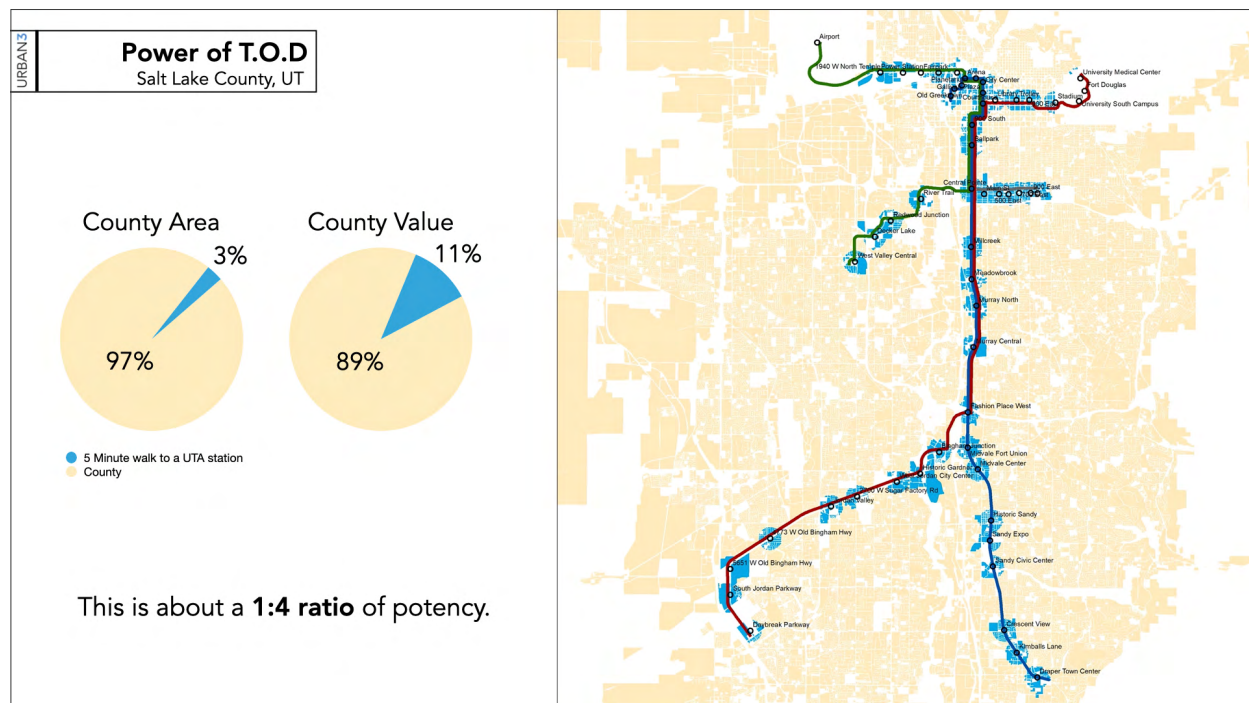
What U.S. local government has investigated the potential and what have they found?⁴

In 2018, Mayor Ben McAdams sought to discover the market value of all public lands throughout Salt Lake County. This would provide insight for County government and the nearly two-dozen cities, towns, and metro townships within Salt Lake County.

The analysis identified sites that may be excluded from development for cultural, geographic, or economic reasons even though they are publicly-owned—sites like the primary airport, steep mountain sides, or other ‘no build’ zones. Even with numerous properties excluded, the analysis still found a remarkable 44 square miles of viable properties.

An assessor’s office usually assigns value to these properties, but the methodology for non-taxable public lands is less-than-rigorous. A more accurate market valuation can be determined by investigating nearby properties. Additionally, GIS technology and macro-market analysis can determine a more reasonable valuation of property, but also highlight “low hanging fruit.”

For example, the region has invested in a tremendous rail transit system. Just the real estate within a five-minute walk from those transit stops is 3% of the county’s real estate, yet it produces 11% of the county’s value. That is a relatively high ratio of 1:4 in land to value potency, and this system connects at least 6 cities in the county. Focusing on publicly-owned properties within this area alone resulted in an impressive opportunity for the county. A simple scenario estimate within these transit walksheds yielded a stunning \$13.5B of valuation gain in these areas, with very conservative estimates of the development of these lands by County government. Additionally, development in these areas could house about 58,000 people and create 39,000 new employment opportunities. This new \$13.5B “book” value is much higher than existing assessed values as it captures the new opportunity value that is already ripe from the public investment in the transit infrastructure. The accompanying graphic shows where this value is located.



⁴ This section contributed by Joe Minicozzi, Principal, Urban3

We undertook the effort to inventory and map all government-owned assets within Salt Lake County and were shocked to discover that assets were valued at roughly \$10 billion. That's huge for a jurisdiction our size. **If we are able to improve the public return on our assets even slightly, we can start to address some of the major challenges facing our region** like increasing the availability of affordable workforce housing and making investments in our transportation infrastructure, and we can do it without raising taxes.

Ben McAdams, Mayor of Salt Lake County, 2013 - 2019

Of course, this is just one example of one redevelopment opportunity within Salt Lake County. When scaled to the whole county, just activating 4.3 square miles of the overall 44 square mile portfolio would result in at least \$45B in new value creation, with associated new revenue streams for the county.

We should note that the benefit is not just financial. Salt Lake County, like many places, has challenges with sufficient housing. Public lands can be used to develop more housing (and commercial areas).

Since the time of the 2018 study, the County has several projects to bring these ideas to fruition.

How do cities manage a UWF?

Cities create a separate organization that exists only to maximize the value of public assets with commercial value, and which is at arm's length distance from short-term political influence. Again, this is not to imply privatization of the assets—just to create a separate organization capable of buffering professional management from short-term politics and to apply the proper commercial tools. This organization can use all the tools available in the private sector to professionally manage commercial assets and apply them to public assets. This approach has its beginnings in the United States at the end of the 19th century, but then the U.S. stopped using this approach, while European and Asian countries developed it further and expanded upon it.⁵

A separate holding company or UWF for public assets could achieve three goals: increase funding of infrastructure or other investments, put investment decisions on a sounder economic footing, and reduce the government's politically motivated access to those assets.

Who appoints the staff of this “UWF,” and to whom are they accountable?

Staff is recruited on merit, often from the private sector. That is where the expertise to manage commercial assets is. It can be thought of as recruitment for a professional sports team: You want to hire a winning team. It should be irrelevant that the team happens to have a government owner.

As with any ownership, the management is held accountable to the board, and the board is accountable to owners. The owners of any government asset are the citizens, and the board is appointed by the local government. However, board appointments should further the goal of maximizing the return on public assets and not be a product of short-term political considerations.

⁵ The US has tended towards a bifurcated path: either wholly privatized or traditional government.

If a city wanted to seriously consider a UWF, what would be a good next step?

Get a rough understanding of the value of the assets that the city owns, both operational and real estate. This can be used to evaluate the viability of a UWF and how much it could contribute to the city budget. The Salt Lake County case study we showed earlier overviews what this kind of analysis can accomplish. The goals of the analysis should include:

- Gain a complete understanding of all publicly owned land
- Project potential market value of public land
- Explore basic scenarios for development
- Estimate revenue impact

What do UWFs have in common with the Green Bay Packers?⁶

The Green Bay Packers is the only publicly owned, nonprofit major sports team in the U.S. The Packers are jointly owned by thousands of fans. The fans vote to elect a board of directors and executive committee but aren't directly involved in football decisions. According to one shareholder, "The benefit that we get is that our team is run by board members. Their only real goal is to make money so the franchise survives, and that happens by the team winning. So we don't have to worry about an owner falling in love with a player in the draft and overriding the general manager." The approach works, as the Packers are one of the most successful franchises in the NFL (including second-most total wins over franchise history), despite being located in a small city.

This is not so different from a UWF, where the owners are the citizens (represented by elected officials) who appoint a professional board/non-executives whose job is to find a coach/CEO who will help them "win" by maximizing the return on public assets. Similar to how an owner can't "override" the general manager for the sake of a favored player, elected officials can't override public managers for short-term political goals.

⁶ Description of Green Bay Packers ownership and quote is from: Kalyn Kahler. "Green Bay Packers, Inc., Owners of the Green Bay Packers." *Sports Illustrated*. July 17, 2018.





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