An Economic History of Zoning

and a Cure for Its Exclusionary Effects

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Abstract (100 words): I outline the twentieth-century history of American zoning to explain how homeowners came to dominate its content and administration in most jurisdictions. Zoning's original purpose was to protect homeowners in residential areas from devaluation by industrial and apartment uses that had been made footloose by trucks and buses around 1910-1920. Completion of the interstate highway system around 1970 made jobs and employees so mobile that suburbs adopted growth controls to stem the tide. If zoning is indeed a substitute for home-value insurance, it seems worthwhile to investigate the possibility of home-equity insurance to reduce the demand for exclusionary zoning.

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This essay offers an economic explanation for the origins of zoning and its twentieth-century evolution. There are two major puzzles to be explained. First, why did zoning rapidly develop in the 1910-1930 era rather than before? Second, why did zoning start to have extraterritorial effects on metropolitan housing prices only after about 1970?

The purpose of this historical inquiry is to offer a test of the thesis of my book, *The Homevoter Hypothesis* (2001). Its central idea is that the way to understand local government behavior is to see it through the eyes of homeowners — and not renters, developers, business interests, or machine politicians — who are resident in the community. Homeowners have a special interest in their community that helps overcome the free-rider problem in public affairs. For most of them, a home is by far their largest financial asset, and, unlike corporate stock owners, homeowners cannot diversify their holdings among several communities. Fear of a capital loss to their major asset and desire to increase its value motivate owners of homes to become "homevoters." They vote their homes in local elections and at public hearings.

The homevoter approach to local government can explain why zoning came into being when it did and why during the 1970s it became more generally exclusionary. New transportation technologies, specifically the bus and truck in 1910s and the development of the interstate highway system in the 1960s, put suburban homeowners at risk from value-reducing development in their neighborhoods and communities. Because homeowners had no means of insuring their assets against these new threats, they and the developers of new homes responded with public land-use regulations that have become increasingly exclusionary. As Albert Breton (1973) first argued (without any subsequent influence, if citations are any measure), zoning is best understood as an alternative to currently nonexistent home-value insurance.

My other purpose in this essay is to explain why a system of home value insurance might be a useful device to deal with exclusionary zoning. Rather than attacking motives for zoning, which are typically unobservable and for which many substitute rationales can be advanced, a more effective remedy would address the underlying financial anxieties that give rise to exclusionary ordinances. Home equity insurance would pay neighbors to a controversial development for any decline in their homes' value caused by the development. This promise would assuage an important anxiety that motivates

residents to oppose new development. Equity insurance addresses without fruitless moralizing what may be the essential problem with exclusionary zoning.

§1. Zoning's Rapid Rise Requires General Explanations

Zoning started in the United States a little after 1910. Many accounts give New York City's 1916 ordinance the honor of being the first comprehensive law, in that it included the whole city in some zone or another (Toll 1969). It is clear, however, that several other American cities were developing similar ordinances at the same time (Fischler 1998; Weiss 1987). Had New York not been first, several other cities were poised to take the title.

Zoning thus was not the product of circumstances in one particular place. Nor, I submit, was it the product of planners who had embraced the City Beautiful Movement, progressives who supported scientific management of government, or lawyers who argued for an expansive view of the police power. Zoning was an idea whose time had come almost simultaneously in cities across the nation. Its origins need to be found in a change in general urban conditions. The roles of planners, progressives, and lawyers were responses to a popular demand for zoning.

Focus on the larger cities for zoning's origins tends to cause modern scholars to overlook that zoning quickly spread to the suburbs and small towns in metropolitan areas. Zoning suburbanized by the 1920s and spread rapidly. Eight cities had zoning by the end of 1916. By 1926, 68 more cities had adopted it, and between 1926 and 1936, zoning was adopted by 1246 additional municipalities (Toll 1969, p. 193; see also McKenzie 1933, p. 300). If these numbers look small by today's standards, it is worth emphasizing that most suburban development prior to 1910 took place within established central-city boundaries or on suburban territory that was quickly annexed to the city rather than independently incorporated (Teaford 1979). Thus the number of independent suburbs who would have occasion to adopt zoning was relatively small and the fraction that did so was impressive.

The village of Euclid, whose zoning ordinance was the occasion of the U.S. Supreme Court's landmark decision to uphold zoning's constitutionality in 1926, was a young suburb of Cleveland at the time of the legal challenge. Euclid's victory cleared the way for zoning in almost all of the state courts, which had been about evenly split on the

constitutionality of zoning up to 1926. A few hidebound courts like New Jersey's continued to resist the zoning tide for a year or two, but the New Jersey Supreme Court's anti-zoning decisions were reversed within a year by a state constitutional amendment (National Municipal Review 1927; Lumund v. Board of Adjustment 1950, p. 584). That New Jersey's constitutional amendment was so quickly and easily adopted in that most suburban of states (its two largest central cities, Philadelphia and New York, are outside the state) is testimony to the suburban enthusiasm for zoning from the outset.

The conventional explanation for zoning's birth invokes the increasing interdependence of urban land-use that arose after the dawn of the twentieth century and the need to deal with incompatible uses by means other than traditional nuisance law and private covenants. This claim is seldom closely argued, which is just as well. Accounts of urban conditions in the eighteenth and nineteenth centuries leave little doubt that the nuisances and near-nuisances that were said to give rise to zoning were much worse in the past (Cronon 1991). If it was just technical externalities that gave rise to zoning, we would have had it a long time ago.

Nor is it credible that no one had thought of zoning before it was imported from Germany, whose cities had adopted it around 1870. Regulation of land use, albeit in a less than comprehensive way, goes way back in American history (Hart 1996), and the extension of regulation to include all land seems like an easily comprehended step. Many eighteenth- and nineteenth-century American cities, not just Washington, D.C., were laid out in detail by their founders (Reps 1965), so urban planning was not new.

§2. The Streetcar Suburbs Set the Stage for Zoning

I submit that a crucial precondition for zoning was the spread of a mechanically powered, intra-urban transportation system. Prior to 1880, most people walked to work in American cities. Horse-drawn streetcars mounted on fixed rails existed in many larger cities before the Civil War, but they were slow, environmentally problematical, and limited in their hauling capacity. As a result, the rich tended to live closest to their jobs, since long walks were irksome as well as time consuming (LeRoy and Sonstelie 1983; Gardner 2001).

The development of electric-powered street railroads in the 1880s made it possible for urban workers to live in exclusively residential districts and commute daily to their jobs in the city. Streetcar lines grew from 3000 miles, all horsedrawn, in 1882 to 22,500 miles of mostly electric lines in 1902 (Cudahy 1990, p. 49). As the streetcar lines were constructed, homebuilders responded to the housing demands of people who could afford the not-inconsequential commuting fares, and the rich started to move to the suburbs.

The rich did not, however, adopt zoning upon moving to the suburbs. The best known history of early suburbanization along trolley lines is Sam Bass Warner's *Streetcar Suburbs: The Process of Growth in Boston, 1870-1900* (1962). Warner offers a detailed account of the development of Boston's close-in suburbs as the streetcar lines were laid outward from Boston's core. He describes the construction of homogenous (as measured by income, not ethnicity) neighborhoods by a highly fragmented, decentralized building industry. Small-time developers built and marketed tracts of homes whose neighborhoods look as if they had been subject to the uniform standards of a zoning law, yet zoning was nowhere in sight. Private covenants were used later in the period, but they typically applied only to the original subdividers' parcel and cannot by themselves account for the uniformity that existed across subdividers' parcels.

Other observers of development in the streetcar era (1870-1910) have remarked on the apparent orderliness of suburban development. Andrew Cappel (1991) describes the outward development of New Haven, Connecticut, in the pre-zoning era. The uniformity with which New Haven's homes were set back from the street, a hallmark of later zoning laws, is striking. Using more quantitative methods, Daniel McMillen and John McDonald (1993) examined the land-use patterns and property values of Chicago just before it adopted zoning. Their calculations led them to conclude that the patterns that zoning subsequently enforced cannot have raised land values, as zoning's proponents argued it would. If zoning is concerned, as its many proponents claimed, with promoting neighborhood uniformity and thus preserving property values, it is not clear why any city would have adopted it during zoning's heyday.

Cappel (1991, p. 632) suggests a reason why land use patterns in the pre-zoning era did not mix apartments and commercial establishments with single family and duplex homes. The impetus for New Haven's suburbanization was, as in Boston, the electric streetcar line. These were enormous improvements over walking and horse-drawn conveyances both in speed and comfort. Apartment houses were almost always built near them to take greatest advantage of the convenience they offered tenants. Streetcars did not carry large amounts of freight, so only less-noxious commercial development, such as retail stores, was pulled out of the central city. Heavy industry remained concentrated around wharves and railheads.

Apartments and commercial activity located near the streetcar lines, making their immediate neighborhoods rather mixed (Alexander Von Hoffman 1996). But it was easy for builders of one and two-family homes to avoid these areas. Residential developers just had to build single-family homes a few blocks away from the streetcar tracks. Moreover, the location of streetcar lines and their stations was subject to public review, and both Cappel and Charles Cheape (1980) found that homebuilders and homeowners used their political muscle to prevent streetcar intrusion into residential or prospectively residential areas. Control over the location of streetcar lines, in other words, was a substitute for zoning.

§3. Trucks and Buses Undermined Informal Land-Use Controls

Cappel found that, in addition to controlling the streetcar lines, homeowners and homebuilders relied on a web of informal agreements, mutual understandings, and ad hoc resort to the law to enforce the patterns that zoning later dictated. Since interlopers and uncooperative developers were only an occasional phenomenon, they could be handled by neighborhood norms that derived from the ineluctable fact that neighbors have to live with one another for a long time. Close observers of land-use perceive the importance of these relationships even today as supplements and sometimes substitutes for land use law (Ellickson 1991; Rudel 1989). The original residents of American streetcar suburbs seemed to have been doing okay without zoning.

I submit that Henry Ford broke up this cozy arrangement. It wasn't the automobile that did it. Ford's Model-T, which appeared in 1908, actually made it easier for middle-class suburban residents to avoid living near the streetcar lines, enabling developers to

fill in the land between the spokes of streetcar lines that radiated from central business districts. It was instead the motor bus and the motor truck, which came into use a few years after the automobile, that undermined the security of suburban, single-family residences.

The truck liberated heavy industry from close proximity to downtown railroad stations and docks. It allowed manufacturers to take advantage of lower-cost land in residential districts. Leon Moses and Harold Williamson (1967) fix the date of the motor-truck revolution in the 1910s, shortly before zoning gained momentum in the 1920s. They found in particular that the cost of over-the-road freight transportation declined during the 1900-1920 period while streetcar fares stayed constant. (See also tables from Historical Statistics of the United States, p. 716, showing a doubling of the number of trucks registered about every other year between 1910 and 1925.)

The motorized passenger bus, another extension of the automobile, likewise liberated apartment developers from close proximity to the trolley tracks in the 1920s. Construction of fixed-rail streetcar lines peaked in 1906. By the early 1920s, jitneys and buses had begun to replace electric streetcars. Streetcar companies themselves began to use buses to supplement and, in lightly traveled suburban areas, supplant trolley lines (Boyer 1983, p. 180; Schaeffer and Sklar 1975, chap. 4). Instead of having apartment builders following the rails, the buses could be depended upon to follow the apartment builders. (Buses could be subjected to public regulation like that of the street railways, but the lower cost of changing a bus route made it more difficult for homeowners in a particular neighborhood to control them. One wonders whether the modern bias towards rail transit rather than more-efficient buses reflects the more limited ability of a fixed rail system to bring unwanted development to residential neighborhoods.)

Newly footloose industrial and apartment developers created a problem for homeowners and the developers who catered to them. A vacant lot in a partially developed neighborhood could now easily be sold to a nonresidential user or an apartment developer. The greater profitability of doing so undermined the patchwork of law and informal relationships that protected homeowners. Cappel (1991, p. 634) notes that homeowners in 1920s New Haven worried that the boom in apartments facilitated

by the new transportation media would overwhelm the prezoning institutions that had protected their neighborhoods. Cappel nonetheless regards New Haven's zoning law as having been foisted on an otherwise contented population by political and planning elites who wanted to put the city in the progressive vanguard (pp. 634-636).

Comments in the 1920s by people without any apparent stake in the planning profession indicate that invasion of residential districts by nonconforming uses was regarded as a serious problem. McMichael and Bingham's respected real-estate treatise, *City Growth and Values* (1923) offered two chapters (of thirty-six) on the new institutions of zoning and planning. The authors, a real estate professional and an attorney in Cleveland, discussed the pros and cons of zoning. Among its most prominent advantages was protection of home values, especially in the suburbs, because zoning forestalled the threat of apartments and commercial and industrial uses from settling in the neighborhood.

By way of illustration of this possibility, McMichael and Bingham displayed two pictures of residential neighborhoods invaded by a natural-gas storage tank and by a warehouse in the pre-zoning era (1923, pp. 316, 318). That this sort of problem was endemic at the time is suggested by a Harvard professor's mention of it in his widely used municipal government textbook (Chester Hanford 1926, p. 234) as well as by state supreme court opinions that upheld zoning at the time (Martha Lees 1994, nn. 179-182). Christine Boyer (1983, p. 156) confirms that such incompatible uses were "commonplace anomalies in the American city of the 1920s."

William Munro (1931, p. 203), a Harvard government professor who had become vice-president of the National Municipal League, pointed out the reciprocal advantages to both residents and businesses of legally-enforced separation:

> With a city entirely zoned, they [realtors] could assure purchasers of residential property that their neighborhoods would never be encroached upon by business, while on the other hand, zoning would give business property a touch of monopoly value. Accordingly the signs went up on vacant lots: "Zoned for business," or Zoned for apartments," with the definite implication that such action on the part of the public authorities had resulted in given the property a higher and more assured value than it would otherwise have.

That potential invasion of residential neighborhoods by incompatible business was a new consideration was suggested by an early zoning advocate, Nelson Lewis (1916). Addressing the issue of zoning, he noted that “a few years ago any plan for such regulations would have had little chance of popular approval, but owners of real estate and building operations appear to realize the danger of unrestricted buildings, and to be ready and anxious to favor action which will prevent further congestion, conserve real estate values, and stabilize the character of districts where that character is desirable and improve it where it is otherwise” (p. 353).

U.S. Supreme Court Justice George Sutherland, hardly an enthusiast of government regulation, raised the possibility of apartment invasion of single-home districts in his opinion in Euclid v. Ambler (1926), still the leading case on the constitutionality of zoning. Sutherland’s mention of apartments is all the more interesting because the plaintiff, Ambler Realty Company, had not even complained about restrictions on apartments. Ambler’s claim was that part of its industrial land along Euclid Avenue (just east of Cleveland) had been zoned for residential purposes. Sutherland brought up the apartment issue on his own (though amicus briefs had addressed it) and uttered the famous metaphor of apartments as “a mere parasite, constructed in order to take advantage of the open spaces and attractive surroundings created by the residential character of the district” (272 U.S. at 394).

It is possible, of course, that contemporary jurists and commentators were being influenced by ideas, such as those of the City Beautiful movement, rather than empirical observation. Yet accounts of the effects of zoning’s adoption suggest otherwise. In an excellent review of American attitudes towards zoning in the 1910-1930 era, Raphael Fischler (1998) quotes many contemporary sources to show that protection of single-family homes was paramount from the outset. Even New York City, whose pioneering ordinance is often regarded as the product of commercial interests, was pressed to protect its residential districts. Fischler’s (1998, n. 48) quote from the New York Times, October 22, 1916, suggests that homeowners were quickly responding to the new assurance:

> Barely three months after the enactment of the zoning code [of 1916], an optimistic headline in the New York Times proclaimed: "Home-Coming Season in Murray Hill — Interesting Changes in Old Center; Many Former

> Residents Moving Back from Uptown — Zoning Act Removes Fear of Business Invasion….

§4. Covenants Had Been Tried and Found Wanting

Fischler describes how protective covenants had been designed to shield the fashionable Murray Hill section on New York City from commerce and apartment development. Covenants succeeded for a time, he noted, because "time honored custom" had prevented commercial development at the edges of Murray Hill (1998, n. 48). The timing of the breakdown of this custom coincides with the development of trucks and buses. After commerce and apartment development began to invade the district, homeowners opted for public controls.

Murray Hill's experience relates to an argument about private covenants as an alternative to zoning. Some modern commentators have advocated covenants as if they had been overlooked when zoning started out (Siegan 1972). Covenants were in fact attempted by large-scale builders in the prezoning years (Weiss 1987). Judges were sometimes hostile to covenants (Ellickson 1973, p. 716), but developers nonetheless did employ them. The problem was that they did not cover enough land area. Nonconforming uses located on the borders of well-planned, covenanted subdivisions, to the detriment of the homebuyers. (One presumes that the transaction costs of acquiring additional land area to provide sufficient protection were large relative to the political costs of initiating zoning.)

Marc Weiss (1987) found that the developers who pioneered large-scale residential subdivisions in Southern California in the pre-zoning era were the prime movers behind the adoption of zoning regulations in Los Angeles. Developers found that voluntary covenants were insufficient to protect their property's value from incompatible uses on their borders. They also took a larger view, according to Weiss, about the possibility that some of their own parcels might be adversely affected by zoning. Developers believed zoning "would maximize aggregate land values, and stabilize values at each location, but would not maximize values everywhere" (1987, p. 101). Far from being something shoved down developers' throats, zoning was actively promoted by developer organizations. Even J. C. Nichols, whose famous Kansas City developments were subject to covenants from 1907 onward, was an early and active advocate of zoning (Worley 1990).

Developer support for zoning was not based on starry-eyed faith in the capacity of planners. It was founded on the need to induce homeowners to invest their savings in a large, undiversified asset. A 1920 zoning advocate pointed out that “So long as undesirable properties could encroach upon an area in which good residences and good income-bearing properties were already established, there would be no stability or trust in real estate as an investment” (Cheney 1920, p. 33). As planning-historian Christine Boyer points out, zoning was seen as a way to provide “an insurance policy that the single-family home owner’s investment would be protected in stable neighborhood communities…” (1983, p. 148).

Modern evidence for the border effect (between subdivisions subject to covenants and their neighbors) that developers worried about is found by Paul Thorsnes (2000). He found that developers in central Michigan sites who could assemble larger subdivisions were able to charge on the order of three percent more per lot for an additional acre of parcel size. (Don’t confuse the size of parcels, the total amount of land to be subdivided, with size of individual lots.) Thorsnes found this particularly strong in rural, unincorporated areas because, he speculated, buyers regarded the private subdivision regulations as a substitute for the less stable zoning regulations in unincorporated areas.

Perhaps as problematic as the vulnerable borders of covenanted land was that covenants seldom controlled an entire municipality. This meant that the fiscal fortunes of homebuyers were left uncertain. A developer of upscale homes could reasonably fear that an adjacent tract of land might be dedicated to downmarket housing. Even if there were no direct spillovers, the buyers in the upscale area would worry about whether their taxes would rise or public services decline if the rest of the land in the municipality were developed for lower-valued properties.

The connection between zoning and municipal fiscal capacity is evident in the many studies finding that low tax rates, ceteris paribus, raise home values (Palmon and Smith 1998). The connection leads municipal leaders to consider that zoning could be used to promote the tax base both by encouraging commerce while making sure that it did not adversely affect home values and other components of the tax base. The report of a

municipal tax committee in Pittsburgh that recommended adoption of zoning in 1916 was explicit:

> If Pittsburgh is to continue to raise practically all its revenues by taxing real estate values, steps must be taken to prevent the needless destruction of those values and to stabilize and promote their increase in every way possible. … Should we any longer tolerate sky-scrapers of unlimited height which steal their light and air from their neighbors, or permit the building of public garages, factories or apartments in splendid residential neighborhoods? (Pittsburgh Committee 1916, p. 20)

The attention to municipal expenditures and the tax base in the Standard State Zoning Enabling Act of 1922 (Fischel 1985, chap. 2) also makes it clear that the progenitors of zoning were thinking well beyond the borders of individual neighborhoods, where property might be protected by covenants. Indeed, there is evidence that covenants and zoning developed side-by-side. In an account of the development of the Cleveland area after the *Euclid* decision, Gerald Korngold (2001) points out that three nearby communities were developed by a single owner and made subject to comprehensive covenants. The municipalities are nonetheless also subject to zoning, and, as if to press home that the two devices are complements rather than substitutes, the covenants are legally administered by the mayors of the three towns. Even where they are comprehensive, covenants may not convey enough control over development to satisfy its residents.

§5. Zoning Perpetuated Metropolitan Fragmentation

The motor vehicle's paternity of zoning led to another offspring, the fragmentation of American metropolitan areas. It is well known and, among many academics and planners, regularly decried that most large American metropolitan areas are governed by scores and sometimes hundreds of local governments. The fragmentation reflects the bottom-up approach to local government that has prevailed through most of American history. It was celebrated by Tocqueville (1835, v. 1, chap. 2) as a source of democratic self-governance in *Democracy in America:*

> The political existence of the majority of the nations of Europe commenced in the superior ranks of society and was gradually and imperfectly communicated to the different members of the social body. In America, on the contrary, it may be said that the township was organized before the county, the county before the state, the state before the union.

Less well known is that for much of the nineteenth century and up to 1910, suburban governments were formed, Tocqueville style, and soon after went out of existence by consolidation with an adjacent, growing central city. Jon Teaford's (1979) masterly review of suburbanization from 1850 to1970 found that until about 1910, it was common for an expanding central city to consolidate (and thus politically absorb) its incorporated neighbors as well as to annex adjacent unincorporated territory. The 1850 to 1910 period was characterized by exuberant incorporations of suburbs around growing cities followed by sober incorporation into the larger body.

After 1910, however a different pattern emerged and began to be the rule by the 1920s. Central cities found that their incorporated suburbs were much more reluctant to give up their independence and consolidate with their large neighbors. In addition, territory that was formerly unincorporated (as part of the county) became more difficult to annex. Residents of unincorporated areas began to consider annexation by the newer suburbs or incorporation as an independent municipality, with no intention of eventually merging with the central city.

I submit that it was the institution of zoning that gave rise to the newfound reluctance of suburbs to merge with their larger neighbor. Prior to zoning, suburbs had to regard urban development and its attendant public costs as inevitable as the tides. There was little to prevent a residential structure from being converted to commercial use, to keep the single-family structure from being subdivided into smaller apartments, or to stop the vacant lot from blossoming with a high-rise apartment building. Few private covenants would cover sufficient area of land within the municipality to afford private control over development.

Given their lack of control over development, suburbs adjacent to the central city must have viewed consolidation as inevitable. As they began getting urban uses and urban densities, they began getting urban service demands. Crime and traffic would overwhelm small-town police forces, and the better-organized, larger forces of the big city became more attractive. Demand for water for domestic use and fire prevention often exceeded local capacity, which was in most places already chancy and irregular. Many central cities had deliberately acquired excess capacity as bait for their outlying areas.

After zoning was developed and began to be accepted in the state courts, suburbs no longer had to view development like that of its urban neighbor as inevitable. A small town could control its land use and fiscal destiny in the face of urban development. Consolidation no longer looked so attractive, and suburbs began cooperating with one another to provide water and other basic services that had scale economies, which had previously been the monopoly of the central city.

Support for the influence of zoning on municipal independence can be seen in histories of municipal incorporation activity. Accounts of twentieth-century municipal formation by Teaford (1979; 1997), Gary Miller (1981), Richard Cion (1966), and William Fischel (2001-H, chap. 10) indicate that incorporations were most often motivated by land use and related fiscal (tax-base protection) issues. This does not mean, of course, that each new city or town wanted to stop development. There were plenty of prodevelopment municipalities formed. But even in them, the residential districts were carefully separated from the fiscally profitable commercial and industrial areas.

Development in western and southern metropolitan areas often occurred in "unincorporated" parts of a formerly rural county. The county almost always stepped in to provide zoning as development took place. In many of the modern municipal incorporations, however, control over land-use was an issue because the county government's zoning was too prodevelopment, especially in its inclination to rezone formerly single-family areas for apartment units (Cion 1966; Fischel 2001-H). Because of their larger size, which makes it more difficult for voters to know candidates' positions, county governments were more often responsive to developer interests and thus were regarded as excessively permissive by owners of homes in existing neighborhoods.

The desire to keep local — read *homeowner* — control of zoning was not only present at the creation of twentieth century municipalities. The chief barrier to metropolitan federalism since the 1920 has been whether the proposed superior government would have control over land use (Teaford 1997). Smaller municipalities are willing to co-operate on many levels with their neighbors, but ceding control over land use within their own boundaries has been a major sticking point for metropolitanism.

§6. Homeowners Became Major Political Players in the Suburbs

So far I have argued that zoning arose because (a) new modes of transportation allowed people to separate where they lived from where they worked and (b) the development of the bus and truck undermined traditional means of protecting neighborhoods. Zoning was preferred to (or added to) covenants because it protected the borders of covenanted land and could protect the municipal tax base and service demands. That ability in turn made it attractive for suburban municipalities to maintain their independence from the central city. The last piece of the puzzle is why homeowners — as opposed to renters, developers, employment interests, and bureaucracies (including planners) — should have taken over as the primary political group whose interests are protected by zoning.

That the detached and (typically) owner-occupied home is at the top of the zoning pyramid is evident in nearly all zoning laws. Early illustrations of this hierarchy in fact draw pyramids with single-family homes forming the apex. The primacy of homeownership remains so widespread that we hardly think of it as something requiring explanation. Yet there is no theoretical reason why other uses of land should be regarded as less important. Apartment dwellers are as much citizens as home dwellers, and renting versus owning has long commanded no special municipal privilege. And the investments, both direct and through employment, that citizens have in commercial, industrial, and public-sector land uses are at least as considerable as in their homes. How did homeowners get the zoning game rigged in their favor?

I submit that the urban transportation revolution that replaced walking with motorized transport led to a less obvious political revolution (Fischel 2001-H). When people walked to work, they had to live close to it. This usually meant that their homes were within the same municipality as their jobs and businesses. In this respect, most urban workers in the walking cities were like most farmers, who still live where they work, and who are of two minds about prospective development: It disrupts their home and business life, but it also provides opportunities for financial gain. Proximity of employment to residence in the pre-1910 walking city meant that local governments were responsive to policies that enhanced their constituents' job-related wealth as well as their residential wealth. Homeowners who lived near their place of business would, in deciding which local

candidate to support, eye the candidate's platform for its effect on their job-related income as well as their residential amenities.

People who moved to independent suburbs and then commuted daily via train, trolley, bus, or car no longer had that binocular vision (Danielson 1976, chap. 2). The city was where they worked, but the suburb, the locus of their residential wealth, was where they voted. Residential amenities — and prevention of anything that smacked of disamenity — became paramount in the eyes of suburban voters.

We know from present-day studies that the value of owner-occupied homes is greatly affected by the things that local governments do (Oates 1969; Grieson and White 1989). Improvements in schools, neighborhood safety, and public parks all raise the value of owner-occupied homes. Conversely, increases in local taxes, local pollution, and ugly billboards all reduce home values.

For most people, an owner-occupied home is the largest single asset they own. The risk of devaluation of this asset cannot be insured, and few homeowners can self-insure by diversifying their other assets for the simple reason that they do not own much besides their house (Caplin et al. 1997). As a result of this, prospective homeowners are careful shoppers. They know that if things go bad in their neighborhood, they will be stuck having paid a lot for an asset that they could sell only at a loss. They can avoid the personal consequences of a school system that has unexpectedly gone bad by moving, but they cannot avoid the financial consequences. Potential buyers can see the declining test scores as well as seller.

The prospect of capital loss or gain influences homeowners' behavior after they have bought and moved in. It makes homeowners, who now constitute two-thirds of the U.S. household population, and even more of the suburban population, especially watchful citizens. They have a powerful financial as well as personal incentive to pay attention to local government land-use policies.

As suburbs formed and became a permanent part of the metropolitan area after 1910, homeowners were motivated to take over local government, or at least the regulatory apparatus. Urban homeownership was growing rapidly in the early twentieth century, especially in the suburbs (Barrows 1983). Homeowners were numerous, well-motivated, and lived in contiguous districts that reduced the transaction costs of political

organization. Having staked their savings in their communities' character, homeowners became a major force in local politics. They supported zoning, which had originally been proposed by homebuilding developers, and they made their homes the primary object to be protected.

This did not mean, of course, that job-creating business was unwelcome in the community. To the extent that it paid local taxes in excess of the additional cost of local services it required, business was welcome in suburbs if its neighborhood effects were not too noxious or it could be sequestered into a nonresidential area of the town. But the mechanism by which the public was persuaded to accept industry was no longer tied to the voter's employment or investment in the business, as it was in the walking city. Public decisions about industrial zoning now focused on things like helping to pay property taxes and minimizing spillover effects that might reduce home values (Teaford 1979).

§7. From Selective to General Exclusion after World War II

The land-use revolution that began in 1916 did not happen all at once, of course. Early zoning laws encountered constitutional and political hurdles that took time to overcome. State courts were, up to the late 1940s, often solicitous of the rights of development-minded landowners (Babcock 1966; Williams 1982). The Great Depression and World War II set back real estate development, so the full impact of zoning was not felt until after World War II.

Nearly all municipalities within the developed parts of metropolitan areas had zoning by the 1950s. Yet zoning's effect on housing cost and general metropolitan development patterns was not much of an issue during that era. Part of this may have been inattention by scholars, but even where the issue would seem to come up, as in government reports about housing, zoning made little impression. It wasn't as if suburbs were open to all. As early as 1953, Charles Haar pointed out the obvious exclusionary intent of minimum house-size standards that were popular at the time and which courts generally upheld.

Even in the late 1960s, when two parallel federal commissions did address zoning issues, the primary complaint was about suburban zoning's effect on the mix of housing and prices within individual communities, not constraints on metropolitan or regionwide

supply (National Commission on Urban Problems 1968; President's Committee on Urban Housing 1969.) Federal commissions that addressed zoning after 1970 have, in contrast, made overall housing prices a major focus (President's Commission on Housing 1982; Advisory Commission on Regulatory Barriers to Affordable Housing 1991). Why did zoning have so little effect on metropolitan housing prices before 1970?

My original take on this was that the unprecedented peacetime inflation that began in 1973 had something to do with it (Fischel 1985, chap. 13). Inflation made new development of the same sort of housing that already existed in the community more of a fiscal burden. Previous residents had financed municipal capital expenditures (water and sewer and streets) at low interest rates. New development required infrastructure that was more costly and could be financed only at interest rates made higher by inflationary expectations. Using the previous methods of financing infrastructure would raise all property taxes, not just those of newcomers. To avoid assuming a greater fiscal burden, I suspected, existing suburban residents tightened their zoning requirements.

The inflation explanation no longer persuades me. Exactions and impact fees could easily have handled the higher costs of new development, so that zoning would not have had to become any tighter. Legal authority for such fees had long been in place (Heyman and Gilhool 1964). More important, as of 2002 we have had nearly two decades of much lower inflation and nominal interest rates than the 1970s and early 1980s, but zoning and the housing-price differentials that appear to arise from it do not seem to have let up. We now seem to have a long-lasting differential in housing prices across regions — California and, to a lesser extent, the Northeast have persistently higher home prices than other regions (Thibodeau 1992; Case and Shiller 1987). These differences did not exist in the 1950s and 1960s. As of 1967, regional differences in prices of new single-family homes were small, and the region that has become the persistent leader in housing prices, the West (dominated by California), then had *lower* prices than either the North-Central and Northeast regions (U.S. Bureau of Census 1969).

It isn't differential growth that causes the new price differentials, either. The population of California, the 1970s leader in the growth control movement, grew much more rapidly in the 1950s and 1960s, but its persistent higher prices did not arise before

the 1970s (Fischel 1995, chap. 6; Gyourko and Voith 1992). Southern states that grew rapidly in the 1970s did not experience housing price inflation. In my survey of the growth control literature, I found little evidence that zoning policies affected metropolitan housing prices before 1970 (Fischel 1990). Something besides inflation seems to have induced a sea-change in zoning behavior in the 1970s.

I believe that during the 25 years after World War II, zoning's impact on suburban development was mitigated by the variety of jurisdictions and that each jurisdiction was able to set its own policies. If Scarsdale was not eager to have more residential or commercial development, then developers could head to the more accommodating suburb of New Rochelle. Most importantly, if the local government of New Rochelle wanted to adopt *pro-development* policies, there was little that a minority faction within the city or anti-development groups outside of the city could do about it. For this reason, the permissive attitude of most courts towards local zoning decisions, under which community decisions were typically upheld if they wanted to retard developer *or* if they wanted to promote development (Williams 1975, chap. 2), had little impact on metropolitan housing patterns. Apartment and commercial developers who were shut out in one municipality simply rolled up their plans and shopped around for another more willing to cut a deal.

By 1970, however, economic and social trends arose that tended to make suburbs as a group more exclusionary. I will divide these factors into shifts in suburban homeowners' demand for exclusion and a movement along the governmental supply curve of exclusion. The demand factors were (a) the growing suburbanization of employment (as opposed to just residence) resulting from the interstate highway system and (b) the expansion of equalitarian legal principles that derived from the civil rights movement. The chief element that facilitated the supply of exclusion was the environmental movement that dawned in 1970.

§8. Interstate Highways Made Businesses and Poor People Footloose

As interstate highways were built in the 1960s, jobs began to follow residents to the suburbs at an increasing rate (Glaeser and Kahn 2001). Suburbs with sufficient amounts of vacant land and residents eager for lower tax-prices accommodated this hegira with the oxymoronic "industrial park" and other zoning innovations (Teaford

1997). The decentralization of metropolitan employment meant that workers no longer needed to live near a single central business district. This undermined the classic urban-economics conception of jobs in a central city surrounded by successively higher-income rings of suburbs. Once jobs suburbanized, low-income workers who had formerly resided close to central cities to conserve on commuting costs now had to find jobs in the suburbs. Indeed, for those poor without automobiles or confined by racial prejudice to the central cities, the “spatial mismatch” between jobs and homes became a real concern (Ihlanfeldt 1997).

Although the suburbs had always been zoned, administration of the rules up to the 1960s was often flexible (Babcock 1966). Land that was initially zoned for three-acre lots as a temporary “holding zone” could be rezoned to smaller lots as development pressure arose. The new development was not much feared by existing homeowners because it was more of the same type of homes that were already there. But as jobs decentralized, the “natural” factors that had established the high-income suburbs — the greater pull for the rich of cheaper suburban land compared to their larger suburban travel cost — started to break down.

Ownership of automobiles grew from 59 percent of all households in 1950 to 82 percent in 1970. The difference in travel costs among income groups was reduced primarily to the opportunity cost of time. Urban miles traveled by passenger vehicles grew by 73 percent between 1960 and 1970, a higher rate of growth than any previous decade (Historical Statistics of the U.S to 1970). As jobs for both rich and poor became decentralized, the poor were almost as inclined to live in a distant suburb as the rich. Just as in the 1920s class segregation by proximity to streetcar lines had been broken by the intra-urban truck and bus, so the income segregation of the suburbs was broken in the 1960s by the increasing use of automobiles and the rapid decentralization of jobs facilitated by new highways.

At the same time, quality of life became a more important issue for existing suburban homeowners, since they, too, were less tied by location near the central city. In the multi-nucleated metropolis, urban jobs are almost equally far from any given suburb. Bruce Hamilton (1982) showed that by the 1970s metropolitan commuting patterns looked almost random when compared to the suburb-to-central-city paradigm.

Communities had come to be chosen more for quality of life than for commuting convenience. The Tiebout (1956) model, in which public services are determined by householders “voting with their feet” among numerous suburbs, became a more realistic description of location decisions and home values (Oates 1969). Nowadays, the local school’s test scores are a larger determinant of home values than access to jobs (Haurin and Brasington 1996).

With a community’s quality of life a more important determinant of home values than location vis-à-vis jobs, homeowners became even more watchful of zoning changes that might affect that quality of life. The formerly relaxed accommodation of development of the 1950s began to harden into a reluctance to rezone. The three-acre minimum lots sizes and farmland categories that had formerly been regarded as “holding” zones solidified into a permanent cast that kept the poor and higher-density development at bay (Downs 1973).

§9. Civil-Rights Lawyers Inspired Suburbs to General Exclusion

Besides job decentralization, the civil rights movement of the 1960s had a profound but subtle effect on suburban land use decisions. The incipient use of zoning to segregate races by neighborhood or community had been struck down in 1917 in Buchanan v. Warley. Maintenance of segregation by the use of private covenants, which were in any case an incomplete substitute for racial zoning (since holdout landowners could sell profitably to blacks), had been legally undermined in 1948 by Shelley v. Kraemer. What was new in the 1970s were the federal and state fair-housing laws that made it more costly to keep blacks out by private discrimination and by informal means, such as racial steering.

Anything that looked like racial zoning was almost never tolerated by the courts. Zoning could, however, be used to reduce potential contact between races, or between high and low income people, by the facially-neutral expedient of insisting on large lots and single family homes in residential districts. Racial anxieties could not, of course, be mentioned in any public document as a reason for the ordinance. Local officials learned quickly to expunge any such language. And, in my opinion, the issue for white suburbanites has rarely been race itself. Zoning in Vermont and New Hampshire, two states with minuscule fractions of racial minorities, does not look much different from

zoning in heterogeneous New York and California. Exclusion is far more an income-based, class issue.

The heirs of the civil rights lawyers recognized that the issue of the 1970s has not just inequality among races, but economic inequality generally. They brought the same legal tools to bear on what they perceived as the maldistribution of wealth created by suburbanization. The new legal targets were no longer segregated schools and overt racial discrimination in housing. They were now inequalities in school spending (Wise 1967) and property tax resources (Coons, Clune, and Sugarman 1969) and zoning laws that made it especially difficult to build private and public housing for the poor in the suburbs (Sager 1969). The legal attack on local property tax financing of schools and the assault on exclusionary zoning were undertaken for the same reason, to open the advantages of suburbs to the less affluent.

As an aside, I would note that the attacks on local school-finance systems have had much greater success than legal attacks on exclusionary zoning. Almost half of the states have had plaintiff victories in the school finance area, and even where suits have been lost, states have responded defensively by centralizing school finance and making differences in property tax bases less important (Hoxby 1997; Joondeph 1995). Yet there is almost no evidence that this has reduced exclusionary zoning.

The evidence to the contrary comes from California. Proposition 13 cut property taxes by half in 1978 and complied with the state supreme court's order to equalize school finance by essentially centralizing all public spending. California homeowners no longer have to worry about the adverse fiscal impact of low-income housing on their tax bills, since Proposition 13 imposed a ceiling on nearly all property tax payments (O'Sullivan, Sexton, and Sheffrin 1995). California communities do not seem to have loosened their zoning laws as a result. Indeed, their increased use of exactions as a substitute for property taxes are said to have made the exclusionary problem worse (Dresch and Sheffrin 1997). There is evidence of a small back-to-the-city movement by affluent parents who send their children to private schools (Downes and Figlio 1999), but there is no evidence of suburbs relaxing zoning laws. Anyone who suspects that reducing property-tax inequality is the key to unlocking the suburban gates has not been

paying attention to California. Middle-class suburban homeowners continue to exclude low-income developments in low-property-tax California as well as everywhere else.

§10. Environmentalism Supplied a Rationale for General Exclusion

The foregoing changes since 1960 — decentralized jobs and civil rights liability — shifted the suburbanites' demand for zoning. The poor were knocking at their gates, and public-interest lawyers were poised to man the battering rams. Zoning's older means of exclusion, which overtly favored single-family homes and discouraged apartments, was newly vulnerable to legal attack. The *Mount Laurel* decisions in New Jersey in 1975 and 1985 served notice that deference to municipal exclusivity, once formerly warmly endorsed by the New Jersey courts and most others (Williams 1975, chap. 5), was now under siege (Haar 1996). Even though *Mount Laurel* itself has not been widely copied, the sentiments it embodies are shared by courts in almost all states.

How did the "supply" of zoning restrictions respond? The suburbs' answer was to adopt the facially neutral policy of restricting all development, not just that for low-income people. The rubric for doing so was "growth management," which became, as Norman Williams (1982, p. 235) put it, "a major movement in the 1970s—apparently springing up spontaneously in local areas all over the country." Faced with the curtailment of selective exclusion, localities began to opt for general exclusion. Moreover, the courts seemed untroubled by this, as shown by the *Mount Laurel* court's dictum:

> "Finally, once a community has satisfied its fair share obligation [a fraction of the region's low-income housing], the *Mount Laurel* Doctrine will not restrict other measures, including large-lot and open area zoning, that would maintain its beauty and communal character"(*Mount Laurel II,* 456 A.2d at 421).

Adopting larger lot and "open space" zoning, two mainstays of growth management, had the drawback of foregoing some fiscally profitable commercial development. For many homeowners, however, that was a fiscally acceptable trade-off. If attracting industry meant having to take the people who worked there, better not to seek it. New commercial development and high-value housing, moreover, were becoming less fiscally profitable in many states as property-tax-base sharing formulas for financing schools were put in place.

Yet anti-growth politics were not easy to supply. Important changes in zoning such as growth controls require a unifying ideology to get them implemented. Economic advantage is a useful private motivator, but it plays poorly in public discourse. Something less obviously selfish is required as a stand-in to get other community residents to rally around the cause. The early twentieth century idealization of the single family home as a font of virtue is said to have helped unify a potentially disparate group, homeowning residents, into a purposeful political force (Lees 1994; Fischler 1998). Home-and-hearth ideology helped state and federal judges, typically drawn from the same social spectrum as suburban homeowners, to suspend their scruples about the new zoning laws' effect on segregating people by their station in life. Judges on both the left and right side of the political spectrum did worry about this in the 1910s and 1920s.

In the 1970s, however, a new ideology was needed to justify the suburban shift from selective growth to reduced growth. Home-and-hearth ideology, after all, applied to the poor as well as the middle class, to the owners of condominiums and mobile homes as well as to owners of standard single-family houses. The environmental movement of the early 1970s provided a seemingly new and compelling ideology to justify a more general exclusion of development. Much of the "limits to growth" literature, which was conceived on an international scale as a computer-simulation project, was quickly adapted to the particulars of local land use (Meadows 1991). "Think globally, act locally" became the unofficial mantra, and acting locally typically means preserving open space from the bulldozer. The mottoes of no-growth, slow growth, managed growth, and (currently) "smart growth" are all facially neutral watchwords which nonetheless are effective substitutes for more selective means of keeping the poor out of the suburbs (Downs 1994).

§11. The Double-Veto System Works Against Development

As I mentioned above, general metropolitan development in the 1920-1960 era was not much affected by zoning because of the variety of local governments. For every suburb that was dedicated to exclusionary zoning there was a not-too-distant town that was more than willing to accommodate development. The pro-development communities were either dominated (for a time) by landowner/developer interests, or they had started out poor enough (as, say, formerly isolated factory towns) that middle

income housing and apartments looked fiscally attractive to them. Where an affluent suburb might reject a middle-income development because of its impact on local schools, a lower-income suburb might see the same proposal as the road to educational salvation. Variety among the suburbs — still falsely presumed to be “homogenous” — ensured that market-driven development had a place to go.

Municipal autonomy in zoning was undermined in the 1970s by several trends that have grown out of the environmental movement. The more universal was the empowerment of neighbors who were dissatisfied with the pro-development decisions of their own local government and its bodies. The legal rule up to the 1970s had been that neighbors usually lose when making these challenges (Williams 1975, chap 2).

The environmental legislation of the 1970s, by which I mean both NEPA and its state-law equivalents and related legislation, empowered private citizens to bring litigation against their own local governments in a different legal setting than the old “neighbors cases” (Frieden 1979). Courts, whose judges share the same environmental attitudes as middle class homeowners (just as 1920s judges shared the ideology of hearth and home) were more sympathetic to claims that the local decision had failed to account for environmental impacts than they had been to seemingly selfish claims that neighbors’ home values were at risk.

Simultaneous with the new empowerment of neighbors was the development of state and regional authorities whose mission was to deal with regional issues (Bosselman and Callies 1971). Such issues either transcended municipal boundaries (e.g., arterial highways) or that spilled over from one municipality to another (e.g., crime prevention). Land use was embraced as one of the regional issues because, as is objectively clear, the natural environment is seldom delineated by municipal boundaries. But regionalism faced (and continues to face) a political problem. As Teaford (1997) showed, regionalism had consistently been rejected after the 1920s because proposed regional governments would supercede local zoning. Individual cities wanted both the right to reject development and to promote it as they pleased.

The regional governance arrangements that began to be formed in the 1970s found a workable compromise. Instead of giving the regional authority plenary power over land use, the systems that evolved were almost all of the “double veto” variety (Fischel 1989;

Popper 1988). A real estate developer had to jump through the regional authority's hoop as well as the local authority's. If he missed either jump, he was out of the running. The regional authority, however, could not make the local authority accept a proposal that the locals had rejected. (The exceptions such as the Massachusetts "anti-snob zoning" act and Portland, Oregon's, metropolitan land-use board, are sufficiently unusual as to prove the rule [Danielson 1976, chaps. 9 and 10; Mildner et al. 1996].) The double-veto structure distinguished the Quiet Revolution from earlier regional proposals, and that made it acceptable to the increasingly anti-development suburbs.

I submit that neighbor empowerment and double-veto systems, in conjunction with local application of environmental laws, changed metropolitan development patterns after 1970. Prodevelopment communities, which had formerly been the suburban safety valves for higher density uses, were less able to accommodate lower-income housing. The fact that the objections to the new development came from a small minority of its own residents or from people who did not live in the community, as at a regional land-use hearing, was now less relevant. The tiny minority and the outsiders now could stop or at least delay and modify (mostly by proposing fewer units) development in communities that had previously offered developers one-stop regulatory shopping.

I do not wish to be entirely censorious of this trend. It is possible that the empowerment of neighbors rectified an unjust situation, one in which majoritarian preferences subsumed the well being of a defenseless few within the community. Putting the necessary but unlovely land use in the poor neighborhood or in the poor community is a classic example of what the 1990s "environmental justice" movement sought to rectify (Lazarus 1992). It is also possible that intermunicipal spillovers sometimes went unaccounted for by those who made land use decisions. Indeed, social scientists have hypothesized a "beggar thy neighbor" syndrome, in which a municipality deliberately zones for fiscally profitable but polluting industries along its downwind or downstream borders (Ingberman 1995).

I say "it is possible" in these cases because the evidence for them is surprisingly slim, especially when compared to the intellectual freight they are made to bear. (They are at the core of the 1970 decision to federalize environmental legislation [Esty 1996].) Studies of zoning board decisions have found that they have been remarkably sensitive

to immediate neighbors' objections, even before neighbors carried the threat of federal environmental lawsuits in their back pockets (Tideman 1969). Modern searches for systematic examples of "environmental racism" have mostly come up short (Been 1994). Likewise, the beggar-thy-neighbor examples often turn out on closer inspection to look more like mutually advantageous deals than one-sided opportunism (Fischel 2001-H, chap. 8).

One reason for optimism in these cases is analogous to why most homeowners try to be civil to their neighbors even if they do not like them. Careless or opportunistic behavior invites retaliation in kind. The numerous and long-term interactions between municipal neighbors cautions the opportunistic types to think about long-term consequences (Gillette 2001). The municipal norm may not be "love thy neighbor," but "respect thy neighbor" is closer to the truth than the opportunistic hypothesis would have it.

§12. Would It Be Better to Discourage Homeownership?

I have so far argued that zoning and the primacy it gives to owner-occupied housing grew out of anxieties on the part of homeowners that more intensive uses would devalue their homes. As residences were moved away from central city jobs, local voters paid more attention to their homes than their business. As jobs in turn decentralized and automobile costs continued to decline, the economic constraints that had once kept the poor tied to central cities made it feasible for them to move to the suburbs. The same civil rights lawyers who had helped tear down the wall of officially adopted racism now turned to the more subtle problem of de facto economic segregation caused by suburban zoning. In response to this, suburbs enlisted the environmental movement to provide an alternative rationale to pull up the gangplank.

My purpose here is not to indict homeowners or environmentalists. I claim membership in the first and sympathy with the second group, and, anyway, it would be like railing against the wind. In fact, the futility of opposing widely popular institutions is what informs my remedy. If the underlying cause of exclusionary zoning is concern about home values, then why not address that concern with a financial instrument and take away (or at least reduce) the exclusionary motive?

One approach is to reduce the incidence of homeownership. The major policy that would accomplish that would be to tax the imputed rent on owner occupied housing. Housing is the largest financial asset that is untaxed by the federal government, and it is possible that homeownership could be reduced substantially from the present 67 percent of all households if the federal government taxed its imputed net rent. Switzerland, the only developed nation to fully tax imputed rent, has the lowest homeownership rate in Europe, 30 percent (Oswald 1996). To tax imputed rent, the government would have to estimate what owner-occupied houses would rent for and then tax the net income (gross rent less property tax, maintenance, depreciation, and mortgage interest) as if it were wages or salaries.

It would not do, incidentally, to simply remove the mortgage-interest deduction, since the remaining equity would still represent an untaxed asset. Owners who paid off their mortgage would enjoy the full subsidy that the present system offers. The encouragement to homeownership would generally be less without the mortgage deduction, but the richest people, who could buy a home with cash, would get the full advantage (Follain and Melamed 1998).

Reducing homeownership is an unlikely policy. Indeed, many important institutions are dedicated to increasing ownership of homes. There are some good reasons for this. The same risk-aversion on the part of homeowners that gives rise to the NIMBY (“not in my back yard”) syndrome and exclusionary zoning also works for more attractive goals. Fear of an adverse effects on homes works its way into all local decisions that affect home values, which is to say, almost all local decisions.

Homeownership motivates childless people to vote for (or at least not vote against) local school bonds that actually improve education (Sonstelie and Portney 1980; Harris, Evans, and Schwab 2001). If you own a home that has more than one bedroom, you are interested in the quality of schools because prospective buyers will be interested in them. Even if you don’t plan to sell soon, your home’s value is the major asset against which you can borrow money. (For those who point to cases where elderly voters do defeat school spending proposals, I ask why all school spending is not locally reduced to its minimum, given that in most places much more than half of the electorate have no children in public schools?)

It isn't just schools that get homeowners' support. Numerous studies have pointed out that homeowners are more involved, watchful citizens than renters, even after one accounts for other differences between the two forms of housing tenure, such as income or race (Davis and Hayes 1993; DiPasquale and Glaeser 1999). They participate more in neighborhood affairs, and their children seem to turn out better (Green and White 1997), just as the single-family zoning advocates of the 1920s said they would.

§13. Home Equity Insurance Might Assuage Homeowners.

The essential question, then, is how to make homeowners less anxious about development in their communities while still retaining the desirable incentives that homeownership provides. The answer I have proposed elsewhere is home equity insurance (Fischel 2001-N). A prototype was adopted in the late 1970s in Oak Park, Illinois, to discourage panic selling in the face of racial transition (McNamara 1984). It has apparently been successful, and some other communities in the Chicago area have adopted it (Mahue 1991). I have been told that developers sometimes pay to enroll opponents to their projects in these programs, which pay the difference between the appraised value and the sale value if it is negative. (The Illinois enabling legislation, available at <www.legis.state.il.us/ilcs/ch65/ch65act95.htm>, describes the procedures.)

Here I am going to state some of the difficulties in undertaking such an insurance scheme to assuage concerns about neighborhood change. I undertake this seemingly self-defeating exercise to justify a concerted public effort in this direction. For if home-equity insurance is the answer, why haven't the creative people who do real estate development and finance come up with it on their own? To put it more bluntly, if I'm so smart (about home values being the key), what ain't' I rich (by investing in a home-equity insurance scheme)?

For a home-equity insurance plan to work, it has to reduce the risks to a homeowner of a particular development that might affect him without otherwise affecting his or the developer's behavior. But home-equity insurance, even more than the regular kind of homeowner insurance, is subject to moral hazard and adverse selection. Robert Shiller and Allan Weiss (1998) have investigated this issue in the context of a metropolitan home value insurance scheme. Their purpose is different from mine. They are

interested in creating home equity markets to insure against metropolitan wide swings in value, so that homeowners don't get trapped in a low value area and become unable to move to a high value part of the country (read California and the Northeast). My concern is far more localized; I am considering home equity insurance for neighborhoods. Nonetheless, the difficulties in establishing home equity insurance are similar.

If companies were to offer home-equity insurance as a third-party financial instrument, they would have to monitor closely the behavior of both developers and homeowners. The reason for this is that some level of NIMBYism is a desirable thing. Planning and zoning officials can seldom learn enough on their own about a given location to be able to tell if a particular development will be a net plus for the community. The present system of relying on the testimony of community members, especially neighbors, has the desirable quality of inducing people to bring out the spillover costs of the development. (It also opens up the developer to the perils of rent seeking, for which the modern "regulatory takings" doctrine might be an antidote [Fischel 1995] but has been set to one side in this article.)

A development that would devalue nearby residences by more than it would increase its own land value should not be done. But if the neighbors were fully insured, they might have insufficient incentive to reveal the adverse effects. A developer might offer to pay the insurance premium for these people to keep them quiet, knowing that the insurance company will cover the loss. To avoid that problem, the insurance company would have to undertake a cost-benefit calculation of every proposed development.

This difficulty is more easily controlled for fires, burglary, or natural disasters. The "moral hazard" in such cases can be managed by the insurance company's insistence on easily monitored precautions, such as installing smoke detectors, putting locks on doors, and building outside of flood plains. But the moral hazard from adverse neighborhood conditions is more difficult to monitor because they are typically unique to a particular neighborhood and the proposed development. The development that could trigger the insurance is, unlike a burglary, often benign. A new convenience store may be a neighborhood benefit in one place, a net cost in another. To winnow the good from the bad developments, the insurance company would have to hire an experienced land

planner to investigate most zoning changes, variances, and other exceptions to the status quo.

Some readers may have already asked themselves why I approach insurance as if it must be offered by third parties. Why not make the developers offer the insurance? They have more information about what can go wrong than most others, so they should be made liable for it. The problem in my view is that both developers and their opponents, the neighbors, would want to have a third-party underwrite the insurance. Developers would want it because their administrative costs would be raised by offering insurance. It is not easy to manage an insurance program. Indeed, one reason the Illinois program was called Home Equity *Assurance* was to avoid the regulations that are imposed on the insurance business in every state.

A more important problem is that neighbors would be skeptical of insurance financed solely by a developer. Development is a notoriously unstable business, and it is easy to imagine the developer going bankrupt prior to the time that insurance payouts would, if justified, actually be due. It may be possible to overcome this with special bonding arrangements, but that again raises the problem of how a third party (who supplies the bond) can determine whether the developer's project is a good neighborhood risk.

The other large barrier to home-equity insurance is the development of a local housing price index on which to base payouts. (The Oak Park scheme and others like it in the Chicago area insure only nominal home values and so require costly reappraisals to deal with inflation. This may not be much of a problem in areas where housing prices do not grow rapidly.) A national or even regional price index would not be enough to determine how much, if at all, a particular neighbor's home has decreased in value as a result of a controversial development. Housing prices rise and fall for all sorts of reasons, and it is clear that prices in one neighborhood can change at a different rate than another neighborhood, even if neither has suffered any localized land-use changes. How would one distinguish a fall in relative home values in a neighborhood because the school-attendance boundaries were changed rather than from the approval and development of a public housing project? Modern econometric techniques can be applied to net out such effects for a large sample of observations, but it is not clear that such results could be applied to individual claims.

The difficulties of developing a home equity insurance market, which I think have prevented it from being developed privately, should not be regarded as insuperable. One should not underestimate the creativity of the financial market to overcome them. The secondary market for mortgages might have seemed like an unlikely possibility prior to its development. Case, Shiller, and Weiss (1993) have made some, albeit halting progress in developing practical metropolitan housing price indexes, and the lessons learned there might inform development of more local indexes. The public costs of undertaking more research and a demonstration project on this should be balanced against the social and economic costs of dealing with or just living with the problem of exclusionary zoning. By most indications, they are not trivial costs.

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