

Flexibility, Justification and Financial Results of Land Development Projects by Local Governments

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Abstract

Land development projects undertaken by local authorities in the Netherlands appear to be an exception to the general rule of cost-underestimation with benefit-overestimation frequently observed in large public projects (Flyvbjerg et al., 2002). In the case of the Netherlands, the profits from municipal land development are larger than the estimated (Korthals Altes, 2010). The exception deserves to be studied, as it may provide with explanations for the budget overruns of other kinds of large projects and inform about their solutions.

In this paper, land development projects are looked at from the perspective of 'flexibility, justification and financial results'. Though public land development projects are seemingly well managed in the Netherlands, local authorities are struggling to make their projects financially and qualitatively feasible, especially in changing market conditions; for example with reduced housing transaction and decreasing building land prices due to the 2007-2008 global financial crisis. In that sense, the following points are shed light on by a case analysis of 'Midden-Delfland's practices from 2008 to 2012; how to incorporate uncertainties and emerging information flexibly in the plan considering its financial implications, how decisions are justified in the process, and how all those points are influencing on the financial end (Faludi and Korthals Altes, 1994).

1. Introduction

Land development projects undertaken by local authorities in the Netherlands appear to be an exception to the general observation in the planning of large public projects that costs are underestimated while benefits are overestimated (Flyvbjerg et al., 2002). In the case of the Netherlands, incomes from municipal land development have been larger than the estimated (Korthals Altes, 2010). This happens in the planning environment where costs and benefits are generally underestimated, however, realized benefits are much higher than actually incurred costs (Korthals Altes, 2010). During the period of 1999 to 2007, the realized annual surplus from land development projects was minimum 1.22 and maximum 2.92 bigger than the budgeted (Korthals Altes, 2010). Besides, the income from land development projects is a relatively important revenue source for local governments in the Netherlands, which accounts for approximately 12% of the whole local government income (Korthals Altes 2008, Allers 2011). While more than 80% of local

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government income depends on grants from the national government (Needham 2007a), either general or earmarked (Figuee et al. 2008), municipal land development gives a room for local governments to exercise their discretion in a way that tailor-made financing mechanisms are made possible in response to local needs.

The recent estimation by Deloitte (2011a), however, presents a different picture. An expected yield on the land development portfolio of all Dutch municipalities in total can be 2.9 billion euro less than what was estimated in the budget of 2010. This loss of 2.9 billion euro is composed of the direct loss of 1.8 billion euro from financially negative plans and the indirect loss of 1.1 billion euro from financially positive plans. This dramatic turn is attributable to the global credit crunch; reduced housing transaction, falling housing construction, decreasing housing prices and subsequently decreasing building land prices (Priemus 2010). Yet, Dutch municipalities are struggling to make their land development projects financially and qualitatively still feasible in the midst of changing market conditions by adopting various micro-adjustments in their project-management (Deloitte 2010). Policies such as the Decree on Budgeting and Financial Reporting (BBV) and Municipal Memorandum Land Policy also provide a municipality with frameworks to manage financial arrangements of land development projects. Those policy-guidelines were formulated before the credit crunch, not necessarily in the prediction of the credit crunch but still relevant to responding resiliently to changing conditions. Those policy-guidelines stand path-dependent on traditional Dutch land development practices.

The Dutch exception with respect to the relation between budgets and realized results of public land development projects deserves to be studied further; why, how and what kind of discrepancies between the budget and the result takes place, and how land development project is managed by the municipality. Since it may provide with explanations for the budget overruns of other kinds of public projects and inspirations for their solutions (Flyvbjerg et al. 2002). Furthermore, it would present more realistic lessons to look at the post-credit-crunch practices of municipal land development, as the post-credit-crunch practices are expected to partly be in the continuation with the ex-credit-crunch practices and partly be innovative. They would reveal more dynamics of changing conditions in which land development projects are operated and of decisions taken by municipalities.

In this paper, municipal land development projects are looked at from the perspective of flexibility, justification and financial results. First, I discuss the concepts of flexibility, justification and financial results used in this paper for analyzing municipal land development based on literature review. Factors that the municipality can influence regarding costs and incomes are briefly explained. Suggested explanations for why municipal land development projects in the Netherlands usually generate surplus over the estimated costs and benefits are also discussed with the introduction to the municipal planning and monitoring cycle of land development projects according to the task division within the municipality. Second, research questions are proposed based on the foresaid concepts with a purpose of a case-study method and an introduction to a selected case. Findings from the case-study are

presented according to the proposed research questions. Third, further discussion points and considerable lessons are suggested based on the case-study findings. What needs to be notified here is that the case-study in this paper is a pilot-study to explore possible research directions further based on collected data and to sharpen the asked research questions for subsequent study based on an identified gap between the questions and what collected data show.

2. Literature Review: Flexibility, Justification and Financial Results of Land Development Projects

2.1 Flexibility

The relation between plan and its implemented result has been an issue in planning studies for a long time (Alexander 1998, Faludi and Korthals Altes 1994, Faludi 1987, Thomas et al. 1983); how much the realized result deviates from the initial plan, what are the reasons for it and how positively or negatively the deviation can be interpreted. One of the main lessons from accumulated case studies is that the initial plan can better be situated in the process of plan implementation as a guideline for further improvements of the plan and its project itself in order to accommodate emerging information and changing conditions (Alexander 1998, Faludi and Korthals Altes 1994, Faludi 1987, Thomas et al. 1983). Thus, flexibility can be defined according to Faludi and Korthals Altes (1994, p.405) as allowing institutional room in the process of project implementation for a possibility of further learning and to reflect newly acquired information on the project, based on the view that ‘the plan can be reconsidered’. Tasan-Kok (2008) distinguishes the use of the concept ‘flexibility’ in the planning literature into three categories; ‘changing decision-making approaches and urban government system’ with such keywords as complexity, multi-actor governance and non-linear decision-making, ‘shifts in urban development traditions and attitude of planning practice’ with such keywords as project-led development, incrementalism and opportunism, and ‘the recognition of diversity, multiculturalism, and heterogeneity as positive aspects of urban society by the planning profession’ with such keywords as diversity and sustainability. Muñoz-Gielen and Tasan-Kok (2010, p.1103) define ‘flexibility’ in their research on public value capturing in urban regeneration projects as a degree of certainty about future building possibilities i.e. what, where and how the landowner is allowed to build and about future contributions i.e. what and when the landowner has to give in kind or in the form of a financial contribution to the concerned planning authority. In this paper, it is meant by flexibility that an initial plan for land development projects can be changing till the completion of the projects. The questions related to flexibility here are why and how changes in the plan were brought about, how those changes in the plan actually improved the project in terms of spatial quality and financial feasibility and what are their consequences on incomes and costs of the projects.

2.2 Justification

The foresaid leads to the following keyword; justification. By justification it is meant what decision makers of public land development projects who bring and approve changes to the plan propose as arguments for such changes to a municipal council which takes ultimate responsibility for its constituency; why those changes are necessary and more beneficial for public interests than without them, as a way of guaranteeing accountability in public policy implementation. Arguments used for justifying decisions show how technical expertise within a project executive body contemplates market conditions, physical constraints or local sentiments. Justifying decisions involved in public land development projects is about choice made on the goal, the design, the contents, the phasing, and the spatial quality of the projects. It is about to find out a balance between the spatial quality to achieve via the project and the financial consequences through the process. Justifications for such decisions are presented in municipal budgets and financial reports which hold the decisions subject to the public debate.

2.3 Financial results

Flexibility is also strongly related to financial results. Needham (2007b) and Korthals Altes (2007, pp.1506) identified the most important financial variables influencing the financial end of a municipal land development project and the possible decision-making areas in the project. Main financial variables are (a) land acquisition costs, (b) costs of site-preparation, (c) interest charges and (d) incomes from land disposals.

Verhage and Needham (1997) identified the cost side and the income side from the point of view of the municipality in more details.

Costs: land acquisition; primary and secondary services; making and supervising the plan; interest costs; possible contribution towards other residential development (for a more extended list of costs, see Muñoz-Gielen, 2010, pp.229-230)

Incomes: revenues from selling serviced plots; possible subsidies from other governmental funds; possible contribution out of local taxes; and possible contribution out of surplus from other projects

Based on the identified financial variables, the scope of choice to the municipality is more elaborated hereunder.

Variable a: the municipality can choose an acquisition strategy;

- Using pre-emption right to acquire future development sites.
- Pursuing an amicable acquisition, using the possibility of compulsory purchase as a big stick (Buitelaar 2010).
- At what price level land acquisition cost would be determined, depending on land ownership situation in the concerned plan area and the bargaining power of the municipality: the price is usually set to be higher than existing use value but same with or less than double existing use value (Needham 1997). In the compulsory purchase law, compensation for expropriation ought to be according to the market price and the market price is likely to be double existing use value (Needham 1997).

- What kind of cooperation-form the municipality chooses with private developers.

Variable b: the municipality can choose the quality and the quantity of services and public facilities delivered within the plan area, and outside of the plan area in relation to needs created by development.

Variable c: the municipality can control or influence the speed and phases of development, determining when to make what kind of costs. The longer a project takes to finish, the more interests are incurred in general. Thus, inflow of incomes can better be expedited as possible and costs can better be incurred later, closer to inflow of incomes. For example, postponement of costs-incurring activities according to actual land disposal schedule can be one of the ways to improve the financial result when acquired land is not likely to be sold soon.

Variable d: the municipality can make a choice on the mix of land uses, cross-subsidizing unprofitable land uses from profitable ones within the plan area. 'More commercial houses' means more profits and 'more social houses' means less profits. By adjusting a development programme, such as types of houses and maximum density, the municipality can influence incomes from land disposal, even though it can hardly influence prices of end-products since the prices are highly determined in the real estate market.

Therefore, decisions made by the municipality influence the financial result of a land development project. How the municipality perceives risks involved in the project, how it interprets the financial status of the project and why and how it chooses to respond to recognized problems in such a way in the process of development; they are to be found in public justifications for such decisions by the municipality.

2.4 Institutional settings: municipal land policy in the Netherlands

There are some starting points to analyse the financial result of municipal land development when looking at it from the viewpoint of flexibility, justification and financial results. From discussion of the financial estimates and results of servicing land by Korthals Altes (2010), it is possible to extract the following explanations for why land development projects by local planning authorities in the Netherlands usually generate surplus over the estimated expenses and revenues.

- 1) Because of flexibility in planning, to adapt to changing conditions by realising the project incrementally in subdivided units and by accommodating emerging information to piecemeal decisions (Korthals Altes, 2010, pp.936 and pp.938).
- 2) Because of conservative accounting rules (BBV) that losses must be recorded in anticipation and profits may only be recorded after realisation so that the principle of prudence in business is encouraged while it is discouraged to justify a cost-overrunning project without making provision for expected losses (Korthals Altes, 2010, pp.934 and pp.938).
- 3) Because of no institutional inducement for land development agencies to show figures that are too positive; in other words, institutional incentives for those

agencies to budget conservatively in order to prevent local authorities from reducing their funding (Korthals Altes, 2010, pp.937-938).

4) Because of buoyant housing market which leads to the option value of future actions, which is especially relevant to the period before the credit crunch, and specific characteristics of local residential market (Korthals Altes, 2010, pp.937-938).

The first point is related to internal factor of the municipal management, namely flexibility in the decision-making process. Here, a budget based on land development plan functions as a financial framework for further manoeuvre in which the project may proceed, focusing on the final quality of the project and not merely on the costs or revenues of the project. Thus, decision-points in one project are not concentrated into a single moment but are spread over time (Korthals Altes, 2010, pp.931 and pp.939). In that way, political influence is to be constantly exercised by checks and balances in the decision-making cycle, rather than decisions are solidified after a certain moment out of the political reach.

The second and the third are related to the way the municipal cabinet presents the budget and the financial result of executed land development projects to the municipal council and the way the municipal council interprets and judges them in order to control and steer development. The fourth point is rather an external factor. The way the municipality is responding to such an external factor is yet determined largely by the first three points. Because the extent that municipalities are affected by the credit crunch may vary from a municipality to a municipality and local scarcity of houses is also different from location to location, it is worth looking at how the municipality perceives the impact of the credit crunch and the status of the local housing market, which would lead to specific adjustments in the project implementation.

Since the first three points are all related to task-division and communication between the municipal council and the municipal cabinet, and also to the administrative cycle of planning and control within the municipality, it is worth mentioning the Dualism in Local Government Act enforced in 2002 and the Decree on Budgeting and Financial reporting enforced in 2004.

The Dualism in Local Government Act gives municipalities a framework in which the distinction between the local council and the cabinet of mayor and aldermen is made clearer. The local council now plays a more independent role in checking and scrutinizing the policy implementation by the cabinet than before. The cabinet consists of mayor and aldermen. They become more professional in local policy formulation and execution because alderman who had formed a member of the local councilors before 2002 become separate from the council and they can now be recruited from outside the municipality according to required expertise in his/her policy field (Severijnen and Bovenkamp Ba 2007).

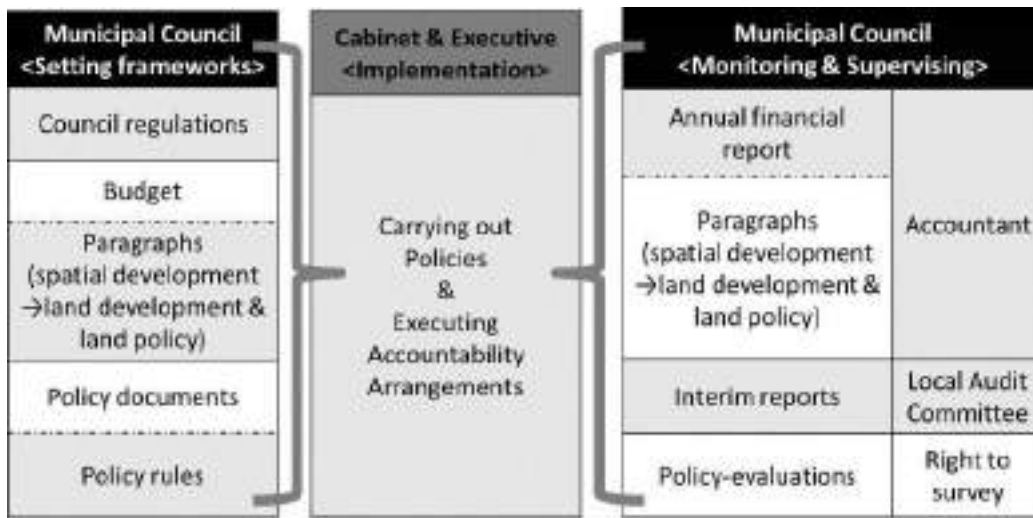


Figure 1: the municipal task division between the council and the cabinet (Deloitte, 2009, pp.10)

The council sets policy-frameworks and the cabinet carries out its policy within the designed frameworks (See figure 1). One of the examples of such policy-frameworks is a ‘Memorandum Land policy’ (Nota grondbeleid), which is tailor-made by each municipality. Main contents of the memorandum land policy are as follows; the aim of land policy, the forms of land policy pursued by the municipality, possible cooperation models for land development with other parties, land acquisition strategies, disposal methods of serviced land, use of reserves for covering possible losses and public procurement principles. The memorandum land policy works in combination with other municipal planning documents such as Strategic Vision (Structuurvisie) and Land Use Plan (Bestemmingplan)² which are mandatory for each municipality to produce, update and conform with, according to the revised Spatial Planning Act.

Based on those planning documents, the cabinet drafts the budget of municipal land development both at a project level and at a municipal level of all projects, carries out the municipal land policy and annually reports the result of its implementation. Annual budgets and annual financial reports drafted by the municipal cabinet are approved by the municipal council (See figure 2). Since 2004, the Decree on Budgeting and Financial Reporting have mandated municipalities to establish a programme-plan or justifiable grounds for the municipal land policy in both annual budgets and annual financial reports.

² Strategic Vision (Structuurvisie) is not legally binding but an indicative plan which globally guides future spatial development, translating other policies of a municipality into spatially-relevant arrangements. Contrary, land use plan is legally binding and contains more detail than the strategic vision.

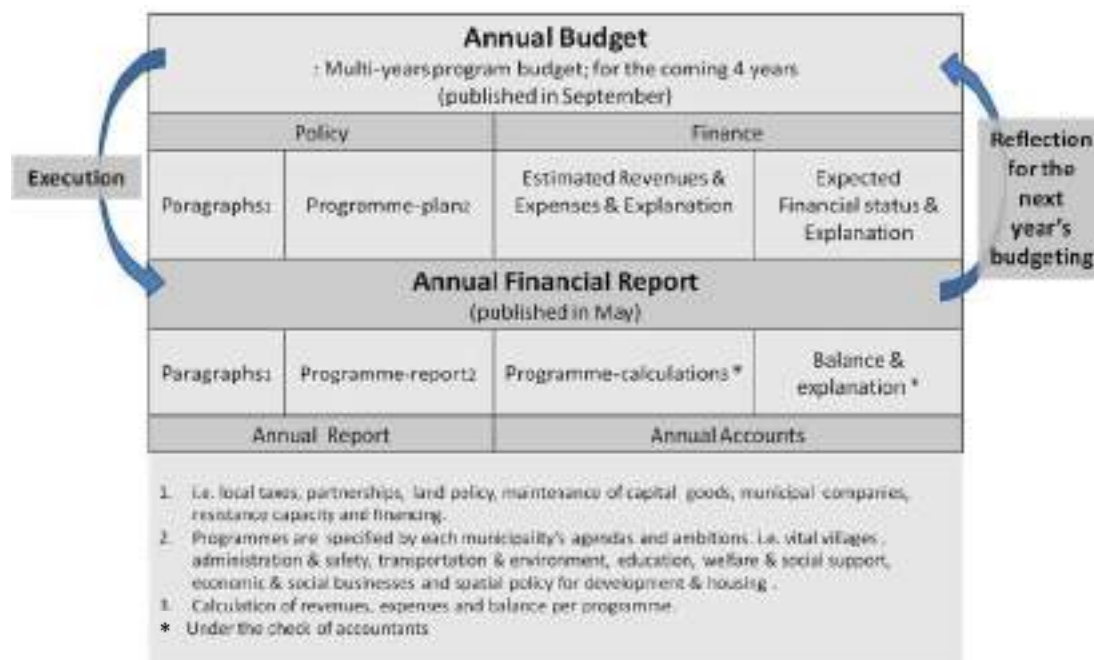


Figure 2: the cycle of planning, execution and monitoring of municipal land development projects and contents of municipal annual budget and financial report (Deloitte, 2009, pp.13)

In the annual budget, the cabinet should state what kind of land policy will be carried out in the next year in order to realize the spatial plan based on the Strategic Vision. Article 16 BBV requires the following items to be explicitly stated in the budget; an integrative vision of the land policy in relation to the realization of the objectives of the programmes which are recorded in the budget, an indication of the way the municipality implements its land policy (active land policy or facilitating land policy), an up-dated forecast of the financial results of the whole land development projects within the municipal boundary with each project's detailed programmes monitored, explanations for estimated incomes and policy principles to run a reserve fund for land development to save generated surplus or to cover possible losses in order to manage risks of land development. Besides, the reasons for a specific policy choice in a specific project should also be stated, since a suitable policy approach can vary from project to project due to each different ownership situation of area in question or available budget.

The annual financial report basically gives an account for the result of how the approved budget is actually spent on, as a reflection on the annual budget. As actual budget execution is carried out at the executive's daily management level, special attention from the council is called for to revisions of land development plans and substantial deviations from the plans. Not all the decisions proposed by the executive require the sanction of the councilors. Still, the councilors are reported of the progress of land development projects, not only by the annual financial report, but

also by the interim communications in a form of either formal or informal hearings and with confidential reports.

3. Case: Midden-Delfland

3.1 Research questions and method

A pilot case study is performed to test the possible research directions based on collected data and to sharpen the asked research questions based on an identified gap between the questions and what data show for subsequent study. Midden-Delfland was chosen for the convenience of access to information and for a relatively small municipal size with dynamic land development, which makes the pilot study possible for a given time; January, February and April 2012 .

Questions are asked as follows.

For the aspect of flexibility:

1) How are uncertainties with emerging information flexibly incorporated in the planning and realization process of land development projects within a municipality considering its financial implications?

For the aspect of justification:

2) How are decisions justified in the process and what are the justifications used?

For the aspect of financial results:

3) How do all the discussed points in the previous questions influence the financial end?

Annual municipal budget documents (Multiyear-programme budget; Meerjarig Programmabegroting in Dutch) published for the year 2009, 2010, 2011 and 2012 and annual municipal financial report documents (Annual report and annual accounts; Jaarverslag en Jaarrekening) published for the year 2008, 2009, 2010 were used to collect data. Except the specified years' documents, it was difficult to get other year's documents in the similar kind when contacting the communication department of the municipality. The contents of the mentioned documents were compared to each other with respect to land development projects and land policy in order to trace back the progress of land development projects and to identify the gradual tendency that the municipality responds to changing conditions such as the credit crunch if there is any mention. Other municipal planning documents such as the Memorandum Land Policy (Nota grondbeleid gemeente Midden-Delfland), Strategic Vision (Structuurvisie), Municipal Housing Policy (Woonvisie; Vitale Dorpen Midden-Delfland 2025), Analysis of the housing market in Midden-Delfland (Wonen in Midden-Delfland 2009-2025; Analyse van de woningmarkt) and interim reports on revisions of land development projects were also referred to. Besides, a semi-structured interview was carried out in February with a planning coordinator who is working for the land development department of the municipality.

3.2 General introduction to Midden-Delfland

Midden-Delfland (hereafter, MD) has a population of 18,225 residents in a relatively spacious area of approximately 50km². Being located next to Delft, and between Rotterdam and The Hague, MD strives to preserve its unique landscape of green pasture in the middle of highly urbanized region. There are three villages, 'Den Hoorn'(7,156 residents), 'Schipluiden'(4,534 residents) and 'Maasland'(6,535 residents), and two neighbourhoods, 'de Zweth' and 't Woudt'. MD aims to provide recreational green space for people living in highly urbanized adjacent areas and to stay attractive for people who want to live there enjoying high quality of life (Gemeente Midden-Delfland 2009b, Gemeente Midden-Delfland 2011f). Faced development pressure in the highly urbanised region, MD has long been active in preserving green landscape by land banking and relocation of glasshouses (van Rij and Korthals Altes 2010, Gemeente Midden-Delfland 2011f). The municipality also tries to balance preservation and development by limiting housing development in the key villages (van Rij and Korthals Altes 2010). Such strategy is called as 'Preservation through development' and its image as 'Vision of Vital towns'. Comparing to other municipalities with a similar population, the municipality has a relatively big scale of land development in terms of a number of projects and capital investment involved.

3.3 Active land policy of MD

Active land policy, in which the municipality acquires land, services and subsequently sell to developers, is called for in order to induce the kind of spatial use desired by the municipality as stated above. The memorandum land policy states the objectives of municipal land policy as follows (Gemeente Midden-Delfland 2009b).

- 1) In order to influence the spatial use.
- 2) In order to influence the spatial quality.
- 3) In order to ensure legitimate distribution of costs and benefits involved in land development.

Those objectives leads to the adoption of active land policy in most projects for the reasons stated in the memorandum land policy as follows (Gemeente Midden-Delfland 2009b).

- 1) In order to ensure cost-recovery by charging costs of site-acquisition and preparation to land disposal prices.
- 2) In order to realise municipal land use plan in an optimized way by the municipality's legitimate rights over land which are derived from holding legal ownership of land.
- 3) In order to use discretionary power when servicing and disposing land to achieve public objectives that cannot be realised by mere application of statutory rules and regulations.

Besides the main use of active land policy, the municipality also uses various forms of cooperation with other private parties, namely, land owners or market developers. Among them are building claim, joint venture, concession, and private self-realisation. The degree of municipal direct influence in servicing land is the highest

in traditional active land policy entailing municipal land acquisition and disposal, and the lowest in private self-realisation. The rest can be classified in between as we see the municipal influence vary in degree.

3.4 Key projects in MD and their relevant features

In order to answer the research questions, relevant points in the course of key projects were reorganized based on the municipal documents of annual budget and financial report (see 3.1 Research questions and method). The following projects are identified as key projects due to their relatively big size or their recurrently emphasized meaning for the municipality. There are far more projects on a smaller scale to be found but the focus will be on the key projects in Den Hoorn and in Schipluiden.

Village Den Hoorn: Look-West, Lookwest-Noord and Kreekzone

Look-West, Lookwest-Noord and Kreekzone are large projects respectively for about 500 houses, 290 houses and an unknown number of houses in Kreekzone. Den Hoorn borders Delft. Thus, the location is regarded relatively more attractive due to the approximation to Delft. At the same time, it is regarded more sensitive to market-competition in the period of the economic crisis since development in the jurisdiction of Delft also generates housing supply.

Village Schipluiden: Keenenburg III and Keenenburg V

Keenenburg III is a project for a new municipality hall of Midden-Delfland and new houses around it. Keenenburg V is a project for development of the area where the current municipality hall is situated. Keenenburg III as mostly green field development and Keenenburg V as redevelopment are related to each other since the planning of Keenenburg V is to fit in with the relocation schedule of the municipality hall.

Table 1: summary of identified key land development projects in MD

	Changed conditions (Key-responding decisions)	Justification used for the key-decisions	Financial result
Look-West In Den Hoorn	a) Technical problems in site preparation (Separation of the problematic subunit) b) Presumably, due to low sales rate of housing in general influenced by the credit crunch (Delay of land disposal and building schedule) c) Extra revenues such as subsidy for public transport connection & tax reimbursement	a) To remove bottlenecks in proceeding the project b) (Description. No justification explicitly stated) c) (Description. No other specific justification)	Positive with an expected profit of approximately 2 million euro

<p>Lookwest-Noord In Den Hoorn</p>	<p>a) One unyielding landowner against land acquisition (Application for an expropriation procedure and finally reaching an agreement) b) The economic crisis and bottlenecks in negotiations with developers on house-types and land disposal prices c) Less costs of site preparation</p>	<p>a) (Description. No other specific justification) b) (Description. No other specific justification) c) (Description. No other specific justification)</p>	<p>Negative with an expected loss of approximately 0.37 million euro</p>
<p>Kreekzone In Den Hoorn</p>	<p>a) Technical problems in site preparation (Separation of problematic subunits from Look-West and Lookwest-Noord and establishment of a separate project) b) Delay in servicing the site and diminished financial result (programme-adjustment from 60% social housing to 30%)</p>	<p>a) To remove bottlenecks in proceeding the projects b) To diminish an expected loss. Because the original plan of 60% social housing has not formally been approved (A strong financial justification. No other options suggested)</p>	<p>Negative with an expected loss of approximately 1.4 million euro</p>
<p>Keenenburg III In Schipluiden</p>	<p>a) Fragmented ownership among the municipality and a group of developers (adoption of building-claim model. Transfer of land from developers to the municipality) b) Technical problems related to peat dikes (re-planning of residential parts of the plan area) c) Extra needs for soil remediation and relocation of public utilities (extra budget-allocation and rescheduling of required work to later)</p>	<p>a) (Description. No other specific justification) b) (Description. Explanation for extra planning costs. No further specific justification) c) (Description. Explanation for extra site-preparation costs. No further specific justification)</p>	<p>Negative with an expected loss of approximately 1.5 million euro</p>
<p>Keenenburg V In Schipluiden</p>	<p>a) Municipal land become vacant and available (developing a residential area and acquisition of the adjacent parcels) b) Insufficient number of social housing in other projects (Increasing a number of social housing)</p>	<p>a) (Description and explanation) b) To compensate a lack of social housing in Keenenburg III</p>	<p>Positive with an expected profit of 0.1 million euro</p>



Figure 3 (left): Look-West project and its sub-plan-units

Figure 4 (right): Subunit 1b, Plan Victoria (Gemeente Midden-Delfland 2011d)

3.4.1 Lookwest: Phasing and parcerlization

The project Look-West is physically close to Lookwest-Noord and related to the latter in terms of the development schedule. After the Look-West had entered into a significant progress, the development of Lookwest-Noord followed to start. Due to its big scale, the Look-West project is composed of several sub-plans. In 2008, a part of Look-west and a part of Lookwest-Noord were consolidated into a separate unit of project, called 'Kreekzone' due to technical problems for servicing the land (Gemeente Midden-Delfland 2008). By separating a difficult subpart of the plan, Kreekzone, it was possible to improve the net present value of the project in 2008 (Gemeente Midden-Delfland, 2008). However, delay in disposing land and subsequently in building from 2009 to 2010 incurred extra planning costs, which is not an insignificant amount contributing to less positive financial result. There was an external subsidy from a regional governmental body, 'Haaglanden', for connecting public transport and reimbursement of value added tax from the national government. The Look-West project is about to finish in a couple of years.

3.4.2 Lookwest-Noord: Difficulties in negotiations and influence of the economic crisis

At the beginning of 2007, a big part of the plan area in Lookwest-Noord was purchased by the municipality (Gemeente Midden-Delfland 2008). There was still one house remaining which needed to be acquired. However, the owner was not willing to sell it to the municipal (Gemeente Midden-Delfland 2008, Gemeente Midden-Delfland 2009c). As a result, the project was impeded. In the end, the expropriation procedure had begun in 2009 (Gemeente Midden-Delfland 2009c) and has not stopped until an amicable agreement was reached in 2010 (Gemeente

Midden-Delfland 2011b). Originally, Lookwest-Noord was expected to yield a positive result with the strategy to diversify house-types. However, negotiations with two project developers starting in 2009 were brought to a deadlock due to disagreement on house-types and land disposal prices. The difficulties are attributable to the impact of economic crisis (Gemeente Midden-Delfland 2009c). In 2010, the impasse in negotiations led to further reduction of the expected result. At the end of 2009, the expected shortage of approximately 0.5 million euro was charged to the reserve of land development (Gemeente Midden-Delfland 2011b, Gemeente Midden-Delfland 2010b). Then, the new calculation in 2011 became positive with 0.13 million euro (Gemeente Midden-Delfland 2011b). Costs of site preparation slightly went down in 2011 due to the more favourable results of public procurement than the estimated.

3.4.3 Kreekzone: Programme-adjustment and plan-optimization

Kreekzone is a deliberately separated unit of project from Look-West and Lookwest-Noord. It was created as a different unit of project, due to technical problems against site preparation found during the development of Look-West and Lookwest-Noord; especially the presence of a 150 kv high-voltage electricity connection (Gemeente Midden-Delfland 2008). It was decided to remove the connection, which would delay in servicing affected areas. In order to avoid the delay of those two projects, the problematic area only was cut from Look-West and Lookwest-Noord, letting the majority of those original plan-areas be steadily developed. Due to the expected negative result of approximately 3 million euro, the plan optimization was proposed in 2010 that the negative result could be reduced to approximately 1.4 million euro by decreasing the initial 60% social housing to 30% in the development programme. (Gemeente Midden-Delfland 2010a, Gemeente Midden-Delfland 2010b). The expected loss of 1.4 million euro was charged to the reserve of land development in 2010 (Gemeente Midden-Delfland 2009a, Gemeente Midden-Delfland 2010a).

3.4.4 Keenenburg III: Increasing losses due to technical problems and subsequent delays

The most of Keenenburg III was owned by the municipality and a group of developers in 2008. In 2008, it was decided to designate a part of the plan area for realizing a new municipality hall. In 2009, the group of developers transferred their land to the municipality and gained the rights to build houses on serviced land. Thus, Keenenburg III is developed in the building claim model (For the building claim model, refer to Needham 2007a, pp. 194). However, technical problems related to peat dikes discovered in the plan area caused substantial delay in further planning in 2008. As a result, parts for residential use had to be re-planned. Accordingly, the historical costs increased so that the project has been expected to yield a negative result since 2009. Extra required work such as soil remediation and relocation of public utilities also worsened the negative result. The expected shortage was charged to the reserve of land development in the annual financial report of 2009 and that of 2010 (Gemeente Midden-Delfland, 2010a, Gemeente Midden-Delfland 2010b). Even

though houses developed in Keenenburg III are targeted at a more expensive price range to increase incomes, the budget-neutral development is not possible.

3.4.5 Keenenburg V: Seizing the opportunity for compensating lacks from other plans

A part of the plan area is a municipal land. The site is currently used for the municipality hall. When it is relocated to the new building in Keenenburg III, the municipal site in Keenenburg V becomes vacant. The municipality is planning to develop the original municipality hall and the adjacent parcels for residential use. In 2010, the percentage of social housing increased compared to an earlier plan in order to compensate a lack of social housing in Keenenburg III (Gemeente Midden-Delfland 2010a, Gemeente Midden-Delfland 2010b). As a result, the expected financial result diminished but still shows a positive amount of 0.1 million euro. An agreement was reached in 2010 on the acquisition of a parcel from other governmental organisation, Service for Rural Areas (Dienst Landelijk Gebied) (Gemeente Midden-Delfland 2010b). Including this, all other planned acquisition has not actually taken place yet (Gemeente Midden-Delfland 2010b, Gemeente Midden-Delfland 2011e).

3.5 Findings

Based on the reorganized course of the key development projects and collected data from a semi-structured interview with a planning coordinator, answers to the research questions are as follows.

3.5.1 How are uncertainties with emerging information flexibly incorporated in the planning and realization process of land development projects within a municipality considering its financial implications?

In the key-projects, information emerged as the projects proceeded. One of the most frequently encountered problems was a technical impediment related to site-preparation which required extra planning and costs (in the cases of Look-West, Look-west Noord, Kreekzone and Keenenburg III). Bottlenecks encountered in negotiations with a landowner and developers and subsequent delays also incurred costs exceeding an initial financial budget (in the case of Lookwest-Noord). Those unexpected events which had negative implications on the financial results in general could not be tackled necessarily in advance but were translated into financial terms as soon as found in order to make fund available for covering any expected losses.

The financial estimation of extra expected costs is required by the Degree on Budgeting and Financial Reporting (BBV). According to the BBV, MD set the rule that an expected loss is charged to the reserve of land development as immediately as the loss is foreseen and that an expected profit can be taken from an original project to the reserve of land development when incomes are greater than remaining expenses to be paid and when it is highly certain to secure expected incomes. Thus,

the reserve of land development functions as a financial buffer for whole land development projects in the municipality in order to cross-subsidize unprofitable land development projects from profitable ones.

In this condition, an initial financial budget based on an initial concept plan functions as a framework for the further progress of the project. It does not necessarily prevent the project from being changed or tried in different directions in response to changed conditions. There is no specific rule to prevent a project from yielding a financially negative result. Aimed spatial quality is sometimes more important than financial result itself. More costs necessary for achieving desirable spatial quality are allowed. Thus, extra incurred costs are tolerated as long as the reserve of land development can cope with expected losses and as long as the municipal council politically declares that the project is necessary and meaningful for the municipality.

With respect to the economic crisis, its negative impact on financial results of land development projects was reflected in general by lowering the annual increase rate of land disposal prices from 3% to 2% for the coming years in the budget of 2012 (Gemeente Midden-Delfland 2011c). For the year of 2010, The annual increase rate of land disposal prices was even fixed as 0%.

3.5.2 How are decisions justified in the process and what are the justifications used?

There are two kinds of decisions in terms of justifications. One requires the sanction of the municipal council in advance. The other is taken by the municipal executive while the municipal council afterwards checks and approves the decisions made. It falls into the former category to establish a new land development project such as Kreekzone as a separate unit of project or to make a new land use plan. Changing details in the boundary of the already approved land use plan falls into the latter category. After the council gives the executive an approval for working on a project, annual plan revision of each land development project is presented to and approved by the council.

The degree of detail in the land use plan is not specified by law so that the land use plan processed in detail can be made and implemented by the executive without asking an approval of the municipal council as long as it fits the overall land use plan (Needham 2007a, p.132-133). Since the land use plan contains what are 'spatially relevant', the financial factors such as the type of houses in the plan and the composition of market and affordable houses in the plan are not necessarily specified in the land use plan. Thus, those financial factors can be adjusted in the process without making a new land use plan which requires the sanction of the municipal council (Needham 2007a, p.155). If the detailed land use plan has already been formally approved, any change of those details specified in the approved land use plan should be referred to the council again. It is one of the reasons why the executive are not likely to have financially-sensitive factors such as the composition of different house types already specified from an initial stage of a project. These

aspects can be found in the case of Kreekzone. As a justification for suggested programme adjustment from 60% social housing to 30%, the executive states as follows.

“The plan optimization is still possible because an original plan of the 60% social housing has not been approved formally.”(Gemeente Midden-Delfland 2010a, Gemeente Midden-Delfland 2011a).

For changes in expected costs and incomes which are highly subject to planning officials' discretion, the executive does not provide specific justification except illustration of kinds of costs and incomes. In general, there is no explanation for why certain costs amount to a specific sum and why certain arrangements of a project are formulated in such a way. For example, justifications for the use of building claim model in the case of Keenenburg III are not found. The arrangements of the building claim model are highly influential on the financial result of the project in general because the arrangements concern at what price range the developers transferred their land to the municipality, on what kind of conditions the developers would get back serviced land including the matter of land prices and allowed house types. They can be commercially sensitive information, of which public availability might damage the bargaining position of the municipality against initial land owners or developers so that the information can better be kept confidential. Yet, it can be questioned why any background information for the adoption of the building claim model are not told which is a crucial factor guiding the financial result of the project in the remaining phases, while other deviations from the previous budget are described in more detail of which the influence is relatively limited on the financial end.

In that vein, it can be questioned about not only what are told for justification, but also not told. For example, only one option was suggested by planning officials to the council, excluding other possible solutions, in the case of Kreekzone when justifying the reduction of social housing from 60% to 30%.

“In this report, we assume that the land development plan will be established in 2010 and that the foreseen loss will be charged to the reserve of land development. Considering the expected loss and the fact that the plan has not been formally established, it was considered if a loss should already be taken in the annual settlement of 2009. For this, possible plan optimizations were sought for. Political and juridical considerations, wills and decision are not taken into consideration when looking for possible plan optimizations.” (Gemeente Midden-Delfland, 2010a, pp.72, Gemeente Midden-Delfland, 2010b, pp.91).

Presentation of one option excluding other possibilities could form cognitive closure for municipal councillors who are supposed to compare possible options and make a political decision as politicians (Hanssen and Saglie, 2010).

The most noticeable justification for the suggested change is financial feasibility. Other solutions such as incorporating more social housing for sale than that for rent or affordable housing targeting at low-middle incomes are excluded here.

Background explanation for the initial scenario of 60% social housing is also missed; why 60% target was set and how it is now justifiable to change it. The original target of 60% social housing was perhaps for compensating a relatively small number of social housing in Look-West and Lookwest-Noord (Gemeente Midden-Delfland, 2009a, pp.90) and for satisfying 30% of social housing at the municipal level based on the municipal housing policy 'Woonvisie; Vitale Dorpen Midden-Delfland 2025' (2010). The municipal housing policy provides a testing framework for determining on house types and residential programmes but its scope is limited to what needs to be realised at a whole municipal level without specifications. Thus, the municipal housing policy states that it is possible to deviate from the criteria of 30% social housing at a project level depending on financial feasibility. That provides planning officials with flexible room to choose a different strategy from project to project. According to the interviewee, it is conventional for the executive to be allowed to deviate from the municipal housing policy if there is a financial reason, given that the council approved the plan.

As explained above, justifications for decisions in land development projects are not all stated in formal municipal documents such as annual budget and financial report. In that sense, the role of elected council members becomes important to ask the executive for accountability. Room for citizens to directly ask accountability or to involve in decisions is relatively limited in terms of access to information and available participation opportunities, except voting and submitting opinions (inspraak procedures). What are not told in formal municipal documents in open access are primarily discussed between the executive and the council. The department of spatial development in the executive takes care of all building projects in the municipality. They suggest or present development initiatives first to the cabinet, the head of the executive, then to the council. Ultimately, those initiatives lead to development programme. The planning officials in the department negotiate with market parties, process the land use plan and translate the plan into financial calculation which is brought to the council. The council confirms the financial and spatial framework of the development. Amendments of the confirmed framework should be referred to the council. Amendments within the confirmed framework can be decided by the cabinet itself. In the described process, the council and more specifically the land policy committee of the council hold several meetings with the executive. The planning officials from the spatial development department explain the progress of projects and answer to questions of the councillors. It is possible to trace back what kind of subjects in the development process they discussed via recorded agendas of the meetings but crucial numbers or detailed information are not usually available in public access.

3.5.3 How do all the discussed points in the previous questions influence the financial end?

Three of the five key projects currently present financially negative results. Delays caused by difficult negotiations with market parties or technical problems in site-preparation mostly resulted in worsened and even negative results than the expected.

However, it was justifiable at the whole municipal level due to the reserve of land development. As long as the reserve of land development could cover an expected loss, it was generously tolerated to exceed an initial budget if necessary. On the other hand, efforts were not necessarily spared to diminish the gap between expected costs and incomes as much as possible, seizing the opportunity to generate more incomes. Thus, dealing with an expected loss is not only depending on the reserve of land development. An internal plan optimization in terms of a balance between financial feasibility and aimed spatial quality should be sought for first. In the case of Keenenburg V, newly available municipal land becomes developed for residential use with the adjacent plots, resulting in a positive result. It is limited with an amount of 0.1 million euro but it is at least helpful to create an extra revenue which would compensate a shortage in its related project, Keenenburg III via the reserve of land development. In the case of Kreekzone, it is expected to diminish an expected loss by reducing a number of social houses.

Expected losses from projects can generously be accepted and allowed because of financial resilience created by the reserve of land development. Thus, available amount of fund from the reserve of land development should be in line with the actual status of land development projects, namely, the amount of losses required to be covered in order to keep the degree of financial resilience at an acceptable level. In the current status, the reserve of land development is decreasing in its size (See figure 5). At the same time, worsening of expected losses from several projects is often observed in the documents of annual budget and financial report, not alone from the identified key projects. If the reserve of land development is not sufficient to cover expected losses, it is possible to make a use of municipal 'resistance fund' (weerstandvermogen) as an exceptional case. The municipal resistance fund is for general use and not dedicated to land development projects. According to the interviewee, it is not expected yet that they have to cover losses from the municipal resistance fund. The currently available fund from the reserve of land development seems to be accumulated mostly before the economic crisis, when a considerable amount of serviced land in Look-West and other projects were sold (See figure 5). However, the historical evolution of the reserve volume and the relation between the reserve and the tendency to more generously accept financially negative projects cannot be analysed here due to limited data.

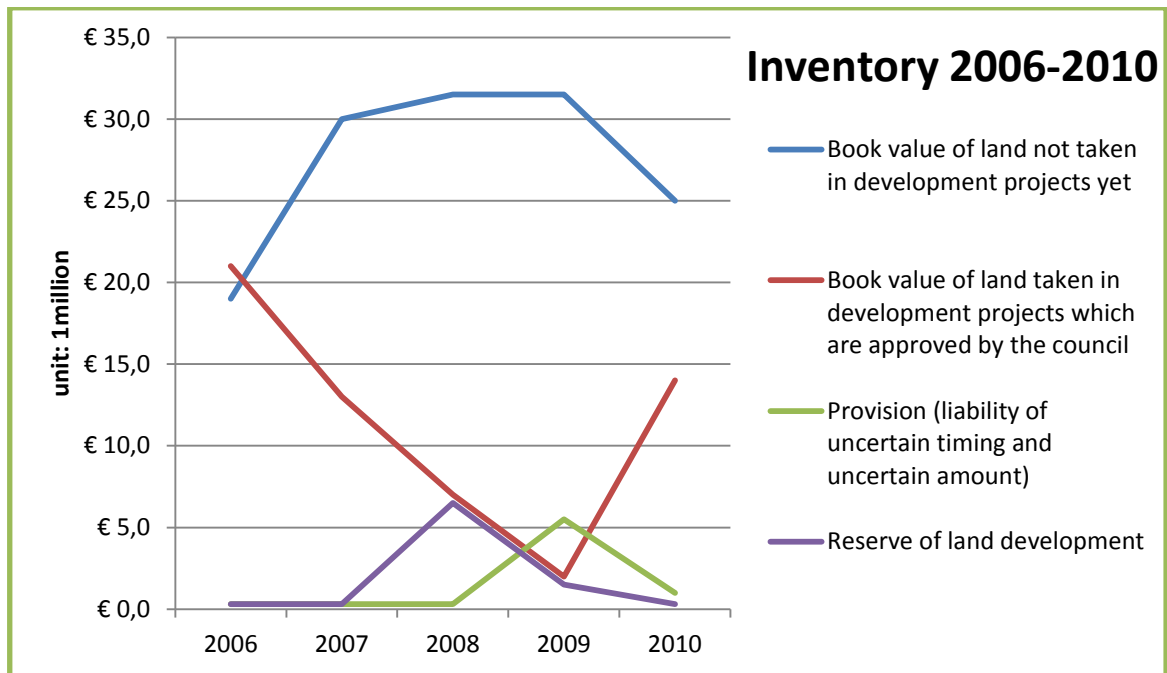


Figure 5: land development inventory 2006-2010 (Deloitte 2011b)

4. Further discussion

Since a pilot case study was intended to test the possible research directions and to sharpen the asked research questions based on the identified gap between the asked questions and what collected data show, some generalizable lessons and further discussion points are presented here based on the findings of the pilot case study.

Flexible decision making is institutionally made possible to improve a project in terms of spatial quality and its financial consequence because an initial plan functions as a framework for further guiding the project. It is made possible by a financial buffer created by the municipal reserve of land development. Even though efforts to improve the project are clearly observed in the identified key projects, those efforts do not necessarily result in a financially positive result but in a less negative result. Unavoidable losses which could not be prevented by plan-optimization are covered by the municipal reserve of land development. The use of the reserve gives the executive flexible room to manoeuvre the project within discretion and also the municipality as a whole to manage several projects related to each other simultaneously. In that sense, the use of the municipal reserve of land development needs to be given extra attention to better understand municipal management of land development projects. It requires more skills and data to analyse the evolution of the reserve of land development as a whole with the status of other projects. An analysis at an individual project level only is not sufficient to understand institutional settings relevant for explaining why certain costs-exceeding is so easily allowed. In order to accommodate emerging new information for adjusting an initial plan which has a financial consequence and to create a financial buffer, the municipal

reserve of land development can be recommended to be applied elsewhere. However, from the perspective of justification, there are some issues to be improved when operating the reserve of land development. No explicit framework for the allocation of fund from the reserve of land development could be observed in the case of MD. The municipal council can better set up principles to prioritize the allocation of the reserve of land development in order to clarify why more losses are allowed for certain projects than others and to set a limit of costs-exceeding so that the executive does not let costs just be accumulated without making possible efforts to tackle them.

The process of justifying decisions regarding land development projects is deeply embedded in ultimate responsibilities of the municipal council to hold the executive accountable. Ordinary citizens are not much involved in such process. In that sense, communication between the municipal executive and the municipal council on municipal land development projects, especially on risks of land development projects seems worth further studying. Even though the results of key negotiations are informed to the municipal council via confidential meetings and reports, a doubt arises whether a confidential form of reporting and communication would be a good way for the municipal council to hold the municipal executive accountable for the best possible performance in reaching their targets in negotiations. The contents of annual budget documents and financial report documents by themselves which are available to the public seem hard to provide enough insights on each land development project since each land development project are not described well as a story of a project from the beginning to the end but more as a collection of annual financial mutations in realizing the project. Then, original intentions to initiate a project and political justifications for such an initiation can easily be missed out from the public discussion on the project. Because each project is discussed annually based on financial mutations taking place in an relevant year, a judgement becomes difficult to be made on whether the project as a whole has been fully optimized or not, as long as there is no description of the full course of the development. If an estimated loss is once covered by the funding from the reserve of land development, the project becomes budget-neutral again in the case of MD. This is a specific way of making a provision for an expected loss among two ways to recognize losses (Commissie BBV, 2012, pp.22). In the case of MD, historical records of loss-covering or revenue-taking are not emphasized much when making a choice on future decisions as long as there is no deliberate reference to those historical records. Reporting is by its nature a retrospective way to ask public responsibilities afterwards. Those historical records are not necessarily to be repeated every time since what happened are not to be reversed anyway. However, it would still be important to trace back the financial records of a project, not only on an annual basis but also on a project basis with its full history in order to accumulate municipal knowledge and lessons for better project operations in the future. At the moment, those knowledge and lessons may be in hands of planning officials in the executive body, but seemingly not in the hands of the municipal council members.

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