The Missing Link in the Evolution of Zoning

Amnon Lehavi

Abstract The centennial of the 1916 New York City Building Zone Resolution provides an exceptional opportunity to reconsider the regulatory and legal basis upon which the key governmental power of zoning is founded. The motive to control the various market externalities embedded in land use regulation, from effects on commercial activity to changes in housing prices, has practically guided local governments in the United States from the very first days of zoning. Yet at the same time, such considerations of market externalities remained in the shadows of explicit zoning law and policy, as the discussion was re-routed to the allegedly more stable foundations of zoning, such as control of environmental, fiscal, or social externalities. This chapter identifies the missing link in the evolution of zoning, showing how the control of market externalities has had an unsung yet powerful impact on the zoning power from its early days.

1 Evolution of Zoning in Retrospect: The 1916 NYC Building Zone Resolution

Zoning was introduced in the United States—and quickly became established—during the first three decades of the twentieth century. Historical accounts of zoning regularly identify three key milestones in its early regulatory and legal development.

The 1916 New York City Building Zone Resolution ("1916 Resolution")[1] is considered to be the first comprehensive scheme to divide an entire city into zones, in which permitted land uses, building volumes, height restrictions, and other details were regulated. The second stage was the nearly uniform adoption of the 1926

This chapter is an updated version of an article titled "Zoning and Market Externalities," *Fordham Urban Law Journal* (2017).

[1] City of New York, Board of Estimate and Apportionment, Building Zone Resolution (adopted July 25, 1916).

A. Lehavi (✉)
Radzyner Law School, Gazit-Globe Real Estate Institute, Interdisciplinary Center (IDC)
Herzliya, Israel
e-mail: alehavi@idc.ac.il

A. Lehavi (ed.), *One Hundred Years of Zoning and the Future of Cities*,
DOI 10.1007/978-3-319-66869-7_3

Standard State Zoning Enabling Act (SZEA)[2] and the 1928 Standard City Planning Enabling Act (SCPEA),[3] through which states granted localities the power to regulate land use. The third prong was the 1926 U.S. Supreme Court decision in *Village of Euclid v. Ambler Realty Co.*,[4] in which the Court validated zoning as falling within government's police power. The Court held that the exercise of the zoning power is constitutionally valid, unless such provisions "are clearly arbitrary and unreasonable, having no substantial relation to the public health, safety, morals, or general welfare."[5]

Over the following decades, federal and state courts generally tended to frame the policy purposes, and consequent legal contours, of the zoning power as falling within the scope of health, safety, morals, and general welfare—with the latter, broad term allowing courts to give local governments significant leeway in exercising their zoning power. While courts have examined whether a particular zoning scheme meets the "substantial relation" test, and have otherwise developed a thick body of law on the potential application of the Takings Clause[6] to the regulation of land use, they have generally refrained from an elaborate analysis of the underlying goals of zoning (Fischel, 2015). When federal and state courts have agreed to dig into the proper purposes of zoning, they have framed the analysis within a certain set of justifications for zoning. These premises focused on the legitimacy of zoning in controlling several types of externalities that may result from the unregulated development of land. As Sect. 2 shows, the types of externalities that courts have focused on are conceptualized in the literature as: (1) technological or environmental externalities, (2) fiscal externalities, and (3) social externalities. In contrast, judges have rarely explicitly addressed the underlying goals for zoning related to "pecuniary externalities" or "market externalities" resulting from unregulated land development. This is so even though such market effects often motivate cities to employ their zoning power.

At the outset, the 1916 Resolution may demonstrate how, alongside considerations of environmental, fiscal, and social effects, the enactment of the Resolution was also practically driven by a concern over market effects. This concern may shed light on the true motives of members of the real estate industry and business owners who were "anxious to put an end to the damages wrought by uncontrolled development." They were joined in their efforts by planning advocates, professional reformers, and public officials, who had different agendas, focusing on environmental and social concerns. Progressives and reformers viewed zoning as a means to limit "untrammeled capitalism" and to make the city more beautiful and livable (Fischler,

---

[2] United States Department of Commerce, Advisory Committee on Zoning, A Standard State Zoning Enabling Act (revised ed. 1926).

[3] United States Department of Commerce, Advisory Committee on City Planning and Zoning, A Standard City Planning Enabling Act (1928).

[4] 272 U.S. 365 (1926).

[5] Ibid., pp. 389–390, 395.

[6] United States Constitution, Amendment V, §3.

1998). The broad coalition in favor of the 1916 Resolution was thus driven by very different motives.

To start with, owners of downtown office buildings increasingly lost their access to sunlight and air to new skyscrapers, thus decreasing their rental value. This loss of sunlight had a dramatic impact, because up until the 1940s, sunlight was the principal source of illumination for interiors (Willis, 1995). The scope of such externalities was considerable: the forty-story Equitable Building, completed in 1915, cast a shadow over four high-value blocks (O'Flaherty, 2005). To control this externality, the 1916 Resolution imposed height limits and setback requirements. As Sect. 2.1 shows, responses to various technological or environmental externalities became the mainstay of zoning concerning both land uses and building restrictions.

A second type of concern that drove the 1916 Resolution demonstrates how technological or environmental issues can become meshed with "social externalities" (presented in Sect. 2.3 below). Owners and operators of high-end retail stores along Fifth Avenue were concerned about the entry of manufacturing lofts, which employed many poor immigrant women. Their fear was that the mass presence of working-class women on the streets would deter the stores' wealthy clientele and undermine the area's appeal. Framed, however, as a problem of incompatible uses, the city was divided into three types of use districts: one reserved solely for housing, another open to commerce, and a third allowing industry (O'Flaherty, 2005). Social segregation was thus indirectly promoted through zoning.

A third problem involved fiscal externalities, namely the growing pressure that the rapid private development of real estate placed on the city's public infrastructure. Both in the financial district and on Fifth Avenue, development caused acute street congestion. Human congestion also posed health threats in both tenement areas and office buildings. Moreover, the congestion issue coincided with the city's effort to unite the five boroughs by an integrated public transit system. Placing limits on building volumes was therefore intended to serve the broader goal of dispersing the population into outer areas, which would in turn facilitate the inter-borough layout of the public transit system (Fischler, 1998).

Further, the constant movement of different populations and activities made it difficult for school authorities to allocate children to particular schools. The mix of land uses also increased the costs of policing, fire-fighting, street maintenance, and postal delivery. The division of the city into use-districts, as well as limiting building volumes, was thus essential to provide more permanent structure to the city's neighborhoods and allow for a well-functioning infrastructure. As Sect. 2.2 shows, fiscal zoning has since then become an explicit regulatory principle.

At the same time, market externalities were also at play as a motivating force for the 1916 Resolution, although their role has been formally overshadowed by the other considerations mentioned above. In 1916, the New York office market went through a period of high vacancy rates, exacerbated by the 1.2 million sq. ft of the Equitable Building (O'Flaherty, 2005). Owners of existing buildings thus wanted to limit new construction that might cause a drop in rents or drive up vacancy rates (Fischler, 1998). Concerns over the stability of real estate values were not constrained, however, to corporate and retail areas in the city. The 1916 Resolution sought also to protect residential properties, and in particular the single-family home, considered to be the apex of the hierarchy of land uses. The motives for doing so included a mix of technological or environmental concerns stemming from incompatible uses; social motives derived from the view of zoning as a "moral system that both reflects and assures social order"; and market-based concerns over the price effect of over-development on existing homes.

Despite the practical effect of market externalities—presented in Sect. 2.4 below—on the motives for the 1916 Resolution and the details of the zoning plan, this purpose has not been explicitly discussed in formal documents published in the aftermath of the 1916 Resolution.

In a speech delivered on November 24, 1916, to members of the National Municipal League, Robert H. Whitten, Secretary of the Committee on the City Plan, Board of Estimate and Apportionment in New York City, elaborated on the purposes and features of the Resolution. Starting with what he considered to be self-evident, Whitten noted: "That a public garage, stable or factory should be permitted to invade and destroy one after another the best residential blocks of the city seems wasteful and foolish" (Whitten, 1917, p. 325). He further stated that regulating the intensity of building development is "essential in order to assure to each section of the city as much light, air, safety from fire and relief from congestion" (ibid., p. 332), again pointing to environmental justifications for the top-down regulation of land development through zoning.

Whitten then explained the ties between the distribution of population and the layout of public infrastructure, and public transportation in particular, addressing both efficacy and costs involved with providing public infrastructure to service residents, businesses, industry and so forth. He thus addressed the fiscal externalities that are mitigated through planning and zoning. Finally, Whitten pointed to social and moral considerations at the basis of the Resolution, stating that "the enlightened civic and moral sense of the community demanded that the former haphazard method of building development should cease and that a comprehensive plan for the control of city building should be adopted" (ibid., pp. 332, 335). However, control of potential market effects was not explicitly presented by Whitten as one of the pillars of zoning.

Differentiating between the various motives for zoning may prove a difficult task in examining individual instances of government action. As Huanshek and Quigley (1990, p. 177) note: "[a]s an empirical matter, it is extremely hard to sort out the pecuniary from the externality motives for zoning." This chore is nevertheless essential, especially to the extent that one type of motive seeks to hide behind another, more defendable ground. This is especially so with pecuniary or market externalities, which have largely remained a legal blind spot, although they play a significant practical role in zoning. Section 2 sets out to analyze each of the aforementioned types of externalities. Section 3 underscores the role of land use regulation in controlling market externalities as the "missing link" in the evolutionary analysis of zoning.

2 Externalities and Theories of Zoning

2.1 Technological or Environmental Externalities

The British economist Arthur Pigou formalized the concept of technological or environmental externalities in the early twentieth century (Pigou, 1932). During the second half of the twentieth century, scholars have increasingly examined the policy and legal implications of such externalities. Since then, this concept has become the subject of extensive scholarship (Sun & Daniels, 2014). Economists define a technological/environmental externality as the "indirect effect of a consumption activity or a production activity on the consumption set of a consumer, the utility function of a consumer or the production function of a producer." The term "indirect" relates to an effect that "does not work through the price system" (Laffont, 2008).

Such externalities can be positive, such as when a firm makes available a new technology or information that allows other firms to manufacture improved products or to cut costs (Dari-Mattiacci, 2009). Negative externalities, which have attracted more attention in the public policy and law context, prominently include adverse environmental effects. Air pollution is probably the best-articulated example. Other technological or environmental externalities, which have a particular bearing on land use, have also been investigated in both theory and practice: noise, groundwater pollution, and the blocking of sunlight or the flow of air (Coase, 1960; Calabresi & Melamed, 1972).

A key point in understanding the role of technological or environmental externalities in land use regulation concerns the intricate ties between the zoning power and otherwise legally actionable harms, such as private or public nuisance. On the one hand, zoning emerged as a top-down regulatory mechanism that controls in advance certain aspects of conflicting land uses, which might otherwise lead to nuisance litigation. Legislatures and courts have explicitly articulated the close ties between zoning and nuisance control from the early days of zoning. As the U.S. Supreme Court famously noted in the *Village of Euclid* case: "a nuisance may be merely a right thing in the wrong place—like a pig in the parlor instead of the barnyard."[7] Zoning is thus justified as a mechanism that spatially orders land uses to minimize potential cases of nuisance.

Accordingly, zoning is intended to save on transaction costs that parties may incur in trying to privately resolve land use conflicts, or on the costs of nuisance litigation. As a doctrinal matter, the fact that an activity is "properly conducted at a place authorized for it under zoning" would regularly shield it from a private nuisance claim, although the case might be somewhat different for some types of public nuisance. One further link between zoning and nuisance control concerns the "nuisance exception" doctrine, which stipulates that some types of land use

[7] 272 U.S. 365 at 388.

regulations might not constitute a taking of property even if they proscribe, without compensation, preexisting activities that amount to “harmful or noxious uses.”[8]

Nevertheless, the zoning power may go well beyond nuisance control (Ellickson, 1973). Zoning regulates various types of technological or environmental externalities that do not amount to nuisances or other civil wrongs.

For example, a zoning decision may impose a density limit to control several issues, including the level of traffic congestion within a development and its vicinity. Nuisance law does not regularly hold a car user liable for the potential externalities she may cause to other residents or drivers because of increased congestion. It is not a type of behavior in which the law identifies a “wrongdoer” engaging in a harmful conduct toward others. In fact, this is a type of behavior in which the law is aligned with Coase’s view of nonconforming uses or externalities as having a “reciprocal nature,” meaning that we cannot categorically identify a “wrongdoer” and a “victim” in such scenarios (Coase, 1960). The solution for the lack of clear guidance by private law mechanisms is provided by regulation. One possible venue is a congestion fee, in which car users internalize the marginal externalities they generate by the payment of a time-based fee (O’Flaherty, 2005). This is feasible for toll roads, bridges, and tunnels, which serve as transportation arteries. However, it is not regularly the case with residential neighborhoods, in which residents are tied to a specific place, meaning that fees would not self-resolve congestion problems. Zoning establishes the level of building density that is seen as appropriate for such developments, also considering on-site and off-site roads, parking, etc.

Zoning thus deals with technological or environmental externalities that go beyond nuisance control. The same holds true for other land use regulations, such as aesthetic controls. Any such regulation would have to meet the “substantial relation” test, set up in the *Village of Euclid* case, but the underlying goals of zoning may well exceed nuisance control.

The role of zoning in controlling technological or environmental externalities thus bears an important lesson for the other grounds for zoning, discussed in the following Subsections. The legitimacy of zoning is not dependent on demonstrating that a certain developer or a person who uses the land engages, or is about to engage, in wrongful conduct (in the private law realm). At the same time, to justify constraints imposed by a zoning scheme, the local government must provide a rationale for the ways in which land uses and building volumes are regulated. Moreover, the farther away from conduct that would otherwise be considered wrongful, the more the municipality would have to ground such constraints in a broad-based rationale. As Sect. 4 will show, this insight has key implications for regulating market externalities through zoning.

[8] This doctrine, while controversial and not fully articulated by courts, originates in the pre-zoning-era case of Mugler v. Kansas, 123 U.S. 623 (1887). The Court refused to apply the Takings Clause to a regulation that prohibited the manufacture and sale of liquor in Kansas, a prohibition that applied also to existing breweries. It reasoned that the regulation stopped an activity that was “injurious to the health, morals, or safety of the community.” In Penn Central Transportation Co. v. City of New York, 438 U.S. 104 (1978), Justice Rehnquist in dissent referred to this exception but described it as applying only to “noxious uses.” Ibid., pp. 144–146.

2.2 Fiscal Externalities

According to the 2012 Census of Governments, state and local governments in the United States continue to rely heavily on their own sources in order to create revenues to finance their expenditures (United States Census Bureau, 2012). For local governments, taxes represent the largest source of general revenue. Property taxes are most prominent, accounting for 73.5 percent of all local tax revenues. Between 2007 and 2012, local property tax receipts increased by more than 15 percent.

The prominence of local revenue—and property tax in particular—for local government finance has always had important implications for land use policy (Lehavi, 2006). In making zoning decisions, local governments may often want to ensure that "households or firms generate a fiscal surplus, not a deficit" (O'Sullivan, 2009). Thus, in considering whether to approve a new zoning scheme, a local government may be motivated to compare its expected marginal expenditures and provision of public services with the expected marginal public revenues.

In the residential context, suburban localities have often resorted to zoning mechanisms, such as minimum lot size or other density limits, to thwart indirect fiscal deficits. Such localities are often especially anxious about households that purchase small-size properties with a value below community average—and thus pay lower property taxes—but otherwise have high demand for public infrastructure, and schools in particular. The practical result of large-lot or other low-density zoning is one in which lower-income households with school age children would be largely left out of the community. In this sense, the fiscal motive plays an essential role in such types of exclusionary zoning. The fiscal tradeoff would be different for high-value properties. The same may hold true for retail businesses that yield not only property tax revenues, but also sales tax receipts (Schwartz, 1997).

The SZEA empowers local governments to engage in fiscal zoning in the residential context, by allowing them to control various aspects of private development, including the size of the lot, a building's height, or its contribution to overall density. Moreover, local governments do not have to ground zoning rules, such as minimum lot size, explicitly in fiscal considerations. The reasons for minimum lot size can also be for positive environmental externalities—because people value open spaces between houses—so that such zoning rules may otherwise promote the *Village of Euclid* case's notion of "general welfare."

In some cases, however, the question of legitimacy of fiscal zoning becomes explicit. The most prominent example is "exactions," requirements that "developers provide, or pay for, some public facility or other amenity as a condition for receiving permission for a land use" (Been, 1991). Notwithstanding the various complications entailed in this body of case law (Fennell & Peñalver, 2014), as most recently expressed in the Supreme Court case *Koontz v. St Johns Water Management District*,[9] the focus of the legal debate on exactions can be conceptualized as involving the legitimate scope of government control over fiscal externalities.

[9] 133 S. Ct. 2586 (2013).

Prior to the *Koontz* decision, the benchmark for the judicial review of exactions was established in *Nollan v. California Coastal Commission*[10] and *Dolan v. City of Tigard*.[11] In *Nollan*, the Court invalidated a California requirement conditioning a building permit for a beachfront property on the owner granting a public easement along the mean high tide line. The Court held that such an exaction lacked an "essential nexus" to the project's anticipated effects.[12] In *Dolan*, the court held that a substantial nexus does exist between a request to expand a hardware store and pave a parking lot and the city's requirement to hand over a piece of the property for a public flood plain and a bicycle path. However, the Court found that the scope of the exaction lacked "rough proportionality" to the expansion's impact.[13] A failure to meet the tests of "essential nexus" and "rough proportionality," respectively, triggers the Takings Clause. The Court based its rulings on the "unconstitutional conditions" doctrine, by which government may not condition the granting of a discretionary benefit on the applicant's waiver of a constitutional right—in this case, payment of just compensation for the property interest in land taken by the city.

In *Koontz*, a 5-4 majority applied the *Nollan/Dolan* framework to a case in which the petitioner was denied a permit request to develop 3.7 acres of privately owned wetland.[14] The denial followed Koontz's refusal to make a payment to finance the improvement of the drainage on another tract, owned by the government. The majority applied the *Nollan/Dolan* standards and the Takings Clause to this required payment, reasoning that "the demand for money burdened petitioner's ownership of a specific parcel of land."[15] This exaction was thus materially different from tax liability. Following *Koontz*, any exaction imposed on a private owner, whether in the form of a property interest in land or a monetary obligation, must meet the essential nexus/rough proportionality standard.

What does the jurisprudence on exactions demonstrate about the legitimacy of land use regulation, aimed at controlling fiscal externalities resulting from private developments? The *Nollan/Dolan* standard validates such a fiscal motive in principle, provided that the measure taken corresponds in both nature and scope to the specific fiscal externality generated by the proposed development. Even under such a heightened standard, therefore, the control of fiscal externalities would be considered legitimate.

A question that remains open in the aftermath of *Koontz* is whether the *Nollan/Dolan* framework applies only to a requirement made on an "ad hoc basis upon an individual permit applicant" or also to a "legislatively prescribed condition that applied to a broad class of permit applicants."[16] If the *Nollan/Dolan* framework is limited to only "ad hoc" or "adjudicative" situations—as the California Supreme

[10] 483 U.S. 825 (1987).

[11] 512 U.S. 374 (1994).

[12] *Nollan*, 483 U.S. at 837–42.

[13] *Dolan*, 512 U.S. at 391–95.

[14] *Koontz*, 133 S. Ct. at 2592–93 (Alito, J.).

[15] Ibid. at 2599.

[16] See California Building Industry Association v. City of San Jose, 351 P.3d 974, 991 (Cal. 2015).

Court recently held[17]—this means that "legislative" land use measures, such as a zoning ordinance, would enjoy the deferential "substantial relation" standard and would not implicate the Takings Clause. In such a case, the legislative measure would have to create a general framework for holding proposed developments accountable to the fiscal externalities they are expected to generate. The challenge for such a legislative measure would not be gaining the legitimacy to rely explicitly on fiscal considerations. It would lie, rather, in the ability of a broad-based ordinance to anticipate the marginal fiscal externalities of a range of specific projects. As Sect. 2.4 and Sect. 3 will show, this is exactly the challenge that applies to the regulation of market externalities.

2.3 Social Externalities

The previous Subsections have already touched on the various ways in which zoning rules, otherwise grounded in considerations of environmental or fiscal externalities, may lead to exclusionary social practices—with low-income households being the usual victims. However, the scope of social motives for zoning exceeds socioeconomic stratification, or even covert issues of race and ethnicity. A municipality, especially one politically dominated by current homeowners, may engage in various methods to preserve social order through zoning. It would be particularly legitimate to do so when those affected by such measures do not belong to a constitutionally protected suspect class, and when the social motive can be complemented by—or even hidden behind—the control of environmental or fiscal externalities.

A notable example is the *Village of Belle Terre v. Boraas* case,[18] in which the U.S. Supreme Court upheld the village's restriction of residential land uses to one-family dwellings based on the ordinance's definition of "family" as "[o]ne or more persons related by blood, adoption, or marriage, living and cooking together as a single housekeeping unit."[19] As a result, a village homeowner was barred from leasing his home to six college students.

The Court rejected equal protection and other constitutional claims against the zoning measure, and relied on a mix of environmental and social externality rationales. It reasoned that "a quiet place where yards are wide, people few, and motor vehicles restricted are legitimate guidelines in a land-use project addressed to family needs." The Court also held that "the police power is not confined to elimination of filth, stench, and unhealthy places. It is ample to lay out zones where family values, youth values, and the blessings of quiet seclusion and clean air make the area a sanctuary for people."[20]

---

[17] Ibid. at 991–92.

[18] 416 U.S. 1 (1974).

[19] Ibid. at 2.

[20] Ibid.

According to the Court, therefore, the negative externalities generated by a house occupied by college students comprise both environmental and social externalities, and the village could legitimately control them. Next to urban problems of congestion and noise, the Court viewed the presence of housekeeping units outside the scope of a "family"—as the zoning measure defined the term—as adversely affecting the village's "values." While controversial, this decision seems to give a mandate to at least some sort of social planning via zoning.

However, social planning via zoning need not be necessarily about exclusion. In fact, the growing phenomenon of "inclusionary zoning" measures, by which localities require or encourage developers to include below market price units in residential projects, is embedded in a concept of positive social externalities. The U.S. Department of Housing and Urban Development (HUD) has long adopted a policy, according to which the "integration of affordable units into market-rate projects creates opportunities for households with diverse socioeconomic background to live in the same developments" and to have access to the "same types of community services and amenities" (HUD, 2013).

Beyond the static concept of social justice, by which low and modest-income households are able to afford housing in high demand areas, the rationale of inclusionary zoning also features a dynamic component that deals with positive social externalities.

An underlying assumption that drives inclusionary zoning is positive synergy between different socioeconomic groups, serving mostly the interests of low and modest-income households, and children in particular, while not harming upper-income households. Mixed-income neighborhoods thus arguably come closer to a socially optimal interpersonal spatial design (Fennell, 2009). While such inclusionary zoning mechanisms have had a fair number of critics, and existing data does not always point to success (HUD, 2011), the positive social externalities remain a driving motivation of housing policy.

A 2015 decision by the California Supreme Court, *California Building Industry Association v. City of San Jose*,[21] highlights both the current features of inclusionary zoning and the way such schemes are viewed as entailing positive social externalities. In 2010, the City of San Jose enacted an inclusionary zoning ordinance, requiring developers of 20 or more housing units to sell 15 percent of the for-sale units at a price affordable to low and moderate-income households.[22] The ordinance offered developers several alternatives to the provision of on-site affordable units—such as provision of a higher number of off-site affordable units, or payment of a substitute fee—but strongly pushed developers toward the on-site alternative. Upholding the ordinance, the Court identified the ordinance's legitimate purposes not only of increasing the number of affordable housing units, but more particularly, of "assuring that new affordable housing units that are constructed are distributed throughout

[21] 351 P.3d 974.

[22] San Jose Municipal Code, §§ 5.08.10-5.08.730.

the city as part of mixed-income developments in order to obtain the benefits that flow from economically diverse communities."[23]

The Court further viewed the requirement to sell 15 percent of the for-sale units at an affordable price as a condition that "simply places a restriction on the way the developer may use its property," similar to other land use regulations or a rent control ordinance, restrictions that do not amount to exactions. The Court reviewed the ordinance under a "reasonable relationship" standard, so that the city did not have to demonstrate the *Nollan/Dolan* nexus between the development and the additional need for affordable housing.[24] Following the *California Building Industry Association* decision, a government's use of on-site inclusionary zoning to promote positive social externalities in mixed-income neighborhoods is not subjected to heightened scrutiny of its fiscal motives.

As a final note, in 2015, New York City's Mayor Bill de Blasio unveiled his plans to enact a citywide ordinance that will require all developers seeking to rezone land for housing to build a specific number of on-site affordable units (Goldenberg, 2015). The inclusionary zoning provisions are "hard, new requirements that for the very first time set a floor for the affordable housing communities are owed in new developments." The focus on on-site units seeks to promote the social externalities of mixed-income housing. The program was approved by the city council in March 2016.[25] Accordingly, the promotion of inclusionary social externalities in New York City is no longer done by ad hoc requirements, but instead through a citywide policy anchored in zoning laws. The promotion of positive social externalities is now explicitly enshrined in the zoning power.

2.4 Pecuniary / Market Externalities

Alongside the analysis of technological or environmental externalities, economists have also considered the role of pecuniary externalities, which work through the price system (Laffont, 2008). In a market economy, certain activities by persons or firms change relative prices or affect the value of assets. These changes create benefits for, or impose costs, on third parties. Economists regularly argue that pecuniary externalities do not affect welfare economics. They suggest that "the ability of new firms to enter an industry and inflict pecuniary losses on existing firms is the process that generates efficiency in competitive markets" (Holcombe & Sobel, 2001). Allowing firms to inflict losses on competitors may be viewed as necessary for economic efficiency. Because market actors have property rights over the resources

[23] 351 P.3d 974 at 979.

[24] Ibid. at 987–91.

[25] New York City, Mandatory Inclusionary Zoning (March 22, 2016). The text of the decision is available at: http://www1.nyc.gov/assets/planning/download/pdf/plans-studies/mih/approved-text-032216.pdf.

they own, but not over their future value, they are not entitled to compensation for pecuniary losses inflicted on them by other market actors.

Over the past decades, however, some economists have acknowledged that in the realistic world of imperfect markets, pecuniary externalities may have welfare effects. Paul Krugman has notably shown that in a world of imperfect competition and increasing returns to scale, pecuniary externalities do matter (Krugman, 1991). Market-size effects are a particular source of pecuniary externalities with genuine welfare impacts, and these in turn have substantial implications for siting choices of firms and the ordering of land uses (Martin & Sunley, 1996).

Krugman examines manufacturers, whose industries, unlike agricultural producers, are typified by increasing returns to scale and a relatively compact use of land. Manufacturers generally prefer to locate factories near their demand markets, because this saves them on transportation costs. The source of the demand, however, does not come only from the agricultural sector or from end-consumers. It is also derived from within the manufacturing sector itself. The result is one of agglomeration or geographical concentration, and it is embedded in positive, reciprocal pecuniary externalities. On the supply side, "manufacturer production will tend to concentrate where there is a large market, but the market will be large where manufactures production is concentrated." On the demand side, firms will tend to "live and produce near a concentration of manufacturing production because it will then be less expensive to buy the goods their central place provides" (Krugman, 1991).

Accordingly, the demand for certain land uses, and the regulatory considerations that need to be taken into account in ordering land uses, might implicate market externalities that have genuine welfare effects. Consider, for example, a plan to rezone agricultural land, located at the fringe of an industrial zone. The developer intends to set up an industrial plant that will manufacture steel products. In deciding whether to approve such a development, the municipality should consider not only technological or environmental externalities, such as increased pollution, or fiscal externalities, such as increased pressure on public roads, but also potential market externalities. If the presence of the steel plant will benefit other industries already located in the adjacent industrial zone—serving both the demand and supply side of the industrial products market—this positive market externality should be considered.

This does not mean, of course, that the concentration of similar land uses will always generate positive market externalities with an overall welfare effect. This is especially true concerning retail businesses, in which the issue of an internal supply and demand of products among businesses themselves is less relevant. Market externalities will apply mostly to the effect that businesses have on other businesses in positively or negatively attracting customers. Several studies have examined the effects of large retail businesses on revenues of other retailers and local employment rates, coming at times to different conclusions: some works seek to document the adverse effects that Wal-Mart stores have on other retail firms and total retail employment (Neumark, Zhang, & Ciccarella, 2008), while other studies show positive pecuniary externalities that large retailers generate for nearby retail establishments (Benmelech, Bergman, Milanez, & Mukharlyamov, 2014).

In a recent study of the effects of big-box retailers on nearby establishments, Shoag and Veuger (2015) offer a theory that seeks to bridge previous studies. They argue that while the overall pecuniary effects of large retailers are positive, directly competing retailers are economically harmed by the presence of a big-box store. The businesses that are positively impacted by their presence are ones that depend heavily on foot traffic, such as small retailers or restaurants. This also means that such positive externalities are negatively correlated with distance from the big retailer, meaning that such positive effects will be particularly significant within approximately a one-mile radius. Moreover, this positive dependence has welfare effects, because many of these affected businesses cannot relocate in the event that the big-box store closes down.

From a broader perspective, localities making zoning decisions should consider three types of market externalities: (1) welfare effects, (2) distributive effects, and (3) "second-hand" off-site environmental or fiscal externalities.

First, developers' siting choices and resulting zoning decisions may yield market externalities with a genuine welfare effect. Importantly, adjacent land users, who may be positively or negatively affected by a decision to rezone land, or to otherwise approve a certain development, should not be seen as having an enforceable individual legal interest concerning market externalities. Adversely affected competitors should not be entitled to block a development because of potential market externalities, the same way that positively affected land users are not in a position to force the municipality to approve the project. Yet zoning goes beyond identifying specific legal interests that may be otherwise enforceable or actionable. Just as considerations of technological or environmental externalities extend beyond the prevention of nuisances that would be otherwise actionable in private law litigation, so do market externalities merit a consideration by local governments if such externalities entail potential welfare effects.

Second, the distribution of positive market externalities, notwithstanding aggregate welfare effects, may also be a legitimate consideration in zoning decisions. Economists have tended to view such distributive grounds suspiciously, suggesting that the political process may allow powerful industries to protect their pecuniary interests at the expense of promoting overall welfare, such as by blocking competing land uses (Holcombe & Sobel, 2001).

As the next Sections show, there is indeed room for concern when decisions driven by market externalities seek merely to serve as an anticompetitive, or an otherwise protectionist measure, at the expense of competitors and other stakeholders. Yet distributive considerations that stem from market externalities should not always be considered normatively inadequate, especially when they are grounded in broad-based policy decisions. To the extent that inclusionary zoning schemes are grounded in such market externalities, and are part of a broad-based policy that addresses access to housing, the consideration of market externalities and their distributive effects may be legitimately weighed in such decisions.

Third, market externalities may also indirectly generate second-hand off-site technological or environmental or fiscal externalities. Section 3 analyzes the effects that a big-box store, such as IKEA or Wal-Mart, may have on small retail businesses located in the city's Central Business District (CBD). A land use decision approving big-box development may create adverse market externalities for nearby businesses. In some cases, the closing down of a critical mass of retailers and related businesses, such as restaurants, may cause the CBD to decline. Such an urban decline may have long-lasting effects that also feature adverse technological or environmental or fiscal externalities—ones that take years and much effort to reverse (Faulk, 2006).

This does not mean that the interests of businesses and other stakeholders in the CBD should always prevail over those of developers, who may have a legitimate business interest in operating somewhere else. Moreover, such developers are not individually responsible for the adverse results of such urban decay, such as physical blight or a decreased sense of security among remaining residents and businesses. No individual legal fault should be attributed to such developers for second hand off-site effects. Yet here too, the zoning power could extend beyond harms that are otherwise actionable in private law to regulate adverse market externalities.

3 The Missing Link: Zoning as Regulation of Market Externalities

Having identified market externalities and their potential effects on land use, this Section underscores the normative justifications for employing the power of zoning to address potential market externalities. It focuses on the use of zoning to control the entry of commercial uses.

Any type of land use regulation that places practical limits on development may generate market externalities. In the housing context, several authors have argued that restrictive regulation is the key variable that explains increasing housing costs (Quigley & Raphael, 2005; Glaeser, Gyourko, & Saks, 2005). Such market effects in the residential context serve the interests of existing homeowners in high demand areas, incentivizing them to influence the political and regulatory process (Fischel, 2015).

Because of the large number and dispersed nature of existing homeowners, and even more so, of adversely affected end users (i.e., prospective buyers/renters), controversies about land use decisions that restrict development formally feature the developer, neighbors, and the local government as the disputants (Ellickson, Been, Hills, & Serkin, 2013). Local governments tend to rely in such cases on explicit considerations embedded in the control of technological or fiscal externalities, and judicial review determines the deference to such considerations.

Matters change, however, when the regulation implicates the entry of commercial uses. The developer will usually have a financial stake in the long-term profitability of the commercial use. For example—the retail revenues that a big-box store would generate over time. At the other end, while some residents or interest groups may object to the project due to environmental or fiscal externalities, current retailers or related businesses would seek to play an explicit role, given the potential market externalities that the development entails. Even if courts deny standing to retailers made anxious by competition, such stakeholders may seek to employ at least one of two tactics: funding litigation for residents or groups with standing, or lobbying the government to protect their interests. In the latter case, if the government supports such interests, it would typically tie its reservations to general concerns over the economic viability of the relevant area or industry.

How should land use regulation draw the normative dividing line between anti-competitive behavior, tailored to promote the particular interests of an existing commercial user, and legitimate broad-based considerations of market externalities? Market externalities should be evaluated along the three dimensions presented above in Section 2.4: (a) welfare effects; (b) distributive concerns; (c) control of second-hand, off-site environmental/fiscal externalities. Additionally, the need to rely on a broad-based consideration in such matters entails both economic and legal considerations.

From an economic perspective, market externalities are inherently the manifestation of a change to a certain preexisting market-equilibrium (Laffont, 2008). This change implicates numerous parties on both the supply and demand sides. An understanding of the geographical scope and the kind of industries affected by the entry of a commercial development cannot rely solely on simple proxies, such as a fixed distance or estimated revenues per square foot. The calculation goes well beyond a zero sum game between existing and future retailers. Evaluating the effects of market externalities requires local governments to have a broader understanding of the commercial activity that takes place within its borders, and how positive or negative market externalities affect not only direct competitors, but also related businesses. As suggested above in Sect. 2.4, the entry of a competing commercial use such as a big-box retailer may have a very different effect on existing retailers than is the case with a nearby complementary business, such as a restaurant.

Moreover, from the point of view of aggregate welfare, I suggest that a regulatory analysis of market externalities—and the effect of a prospective development on the economic viability of preexisting commercial activities—requires the municipality to take a general stand on matters that are at the basis of agglomeration economics. For example, does the city place a special value on downtown business districts that feature a multitude of small and medium-scale retailers, or does it prefer retail economy concentrated at its perimeter?

The same dilemmas also touch on the two other dimensions of market externalities. A decision by a local government to prefer small and medium-scale businesses to large-scale retailers because of distributive considerations must consider the implications of a regulatory decision on other small businesses that are not direct competitors of the prospective large retailer, and which may be generally better off locating near such big businesses. If the city wishes to differentiate between various types of businesses in its distributive agenda—e.g., it seeks to preserve small fashion stores but it is less concerned about protecting mom-and-pop restaurants—it should not only offer a normatively valid reason for this differential treatment of small businesses, but also design its commercial zones to achieve such a result. The same requirement for a broad policy should apply to the control of second-hand environmental externalities or fiscal effects. If the city is determined to decrease the prospects that its CBD will become rundown, it should have an explicit policy on what types of businesses are inherently essential for the economic viability of the CBD as a whole, or particularly prone to market externalities.

From a legal perspective, a broad-based policy regulating the entry of commercial uses, due to considerations of market externalities, is justified because existing private-law mechanisms (such as nuisance law) may fail to resolve certain types of externalities. As suggested in Sect. 2.1, the farther away one moves from land uses that may otherwise constitute a wrong in private law, the greater the burden on the local government to ground its restrictions in a broad-based policy. Of all externalities, market externalities are most often reciprocal—to use Coase's term—in identifying the normativity of the conduct. Therefore, to the extent that a land use regulation limits the entry of a commercial use because of market externalities, the regulation must show how such a decision promotes the *Village of Euclid* decision's concept of general welfare in the most genuine sense,[26] and why such a decision is not merely a pretext for preserving the status quo in the service of a politically powerful economic actor. Even within the "substantial relation" deferential standard, a legal limit based on market externalities must rely on a credible broad-based policy.

These insights may be instrumental in delineating the normative dividing line between legally inadequate protectionism and a legitimate control of market externalities, even if existing businesses may benefit from limits on entry of commercial uses in both cases.

Consider, on the one hand, the legal controversy over zoning limits placed on the entry of "formula businesses," typified by a "standardized array of services or merchandize, trademark, logo, service mark, symbol, decor, architecture, layout, uniform, or similar standardized feature."[27] This term seeks to capture major national retailers, such as Wal-Mart, McDonalds, or Starbucks.

Numerous municipalities in the United States have placed limits on such retailers, subjecting them to special permit procedures or economic impact reviews (Ellickson et al., 2013). The reasons provided for such limits are usually grounded in preserving an appropriate balance of small, medium, and large-scale businesses, or in controlling other effects that such retailers may have on the community. However, courts have scrutinized such regulations, especially when similar limits were not placed on other large businesses that do not have standardized features, meaning that the true motive for such limits is a targeted policy against specific retailers, not a general policy on the preservation of small businesses, or the viability of the CBD.[28] This targeted policy in the guise of a market externality analysis is especially prominent

[26] 272 U.S. 365 at 388.

[27] See Island Silver & Spice, Inc. v. Islamorada, 542 F.3d 844, 845 (11th Cir. 2008) (quoting the language of Ordinance 02-02 §§ 6.4.3-4(a-b), adopted in 2002 by the City of Islamorada, Florida).

[28] Island Silver & Spice, 542 F.3d at 847–49 (reasoning that the goal of preserving Islamorada's "small town" features does not stand if other large non-standardized retailers are allowed, and holding that the special limits on formula retail violate the Dormant Commerce Clause's protection of interstate commerce).

in the context of Wal-Mart, where labor unions seek to use municipal zoning regulations to prevent the entry of Wal-Mart stores (Epstein, 2007).

On the other hand, courts have been more deferential to zoning regulations that are grounded in a broad-based policy. In *Hernandez v. City of Hanford*, the California Supreme Court upheld a 2003 amendment to the city's zoning ordinance.[29] Aimed at protecting the "economic viability of Hanford's downtown commercial district," typified by a large number of "regionally well-regarded retail furniture stores," the original ordinance previously prohibited the sale of furniture in another commercial district, the PC district. The amendment created a special exception for large department stores—those with at least 50,000 sq. ft of floor space—located in the PC district, allowing them to sell furniture within a specifically described area of no more than 2500 sq. ft within the department store. In doing so, the amendment sought to add to the original goal of preserving the economic viability of the downtown commercial district, a new goal of attracting the "type of large department stores that the city views as essential to the economic viability of the PC district."[30]

The court viewed both goals as legitimate purposes, and validated the zoning measures taken to attain them. Surveying the history of the zoning ordinance and its amendments, the court noted that when the PC District was established in the late 1980s, a city committee identified types of commercial uses already established in the downtown district and which the city did not want moved to the PC district. These uses include car dealerships, banks, professional offices, and furniture stores.

The court concluded that the zoning power extended to the regulation of economic competition to advance a legitimate public goal. It held that a zoning ordinance is not necessarily invalid because it has the effect of limiting competition. Zoning actions, in which the "regulation of economic competition reasonably could be viewed as a direct and intended effect," would be valid as long as the primary purpose is a "valid *public* purpose such as furthering a municipality's general plan … for localized commercial development" rather than simply serving a business's private anticompetitive interests.[31]

Thus, for example, a city's decision to limit the entry of discount superstores and to organize its commercial development in existing neighborhood shopping centers would be legitimate, even if it has a "direct and intended effect of regulating competition." Such a zoning would be valid as long as it serves legitimate purposes such as maintaining the "vitality and economic viability of the city's neighborhood commercial centers," and thus avoiding an "urban/suburban decay" that might result from the shifting of commercial activity.

In this case, in working to preserve the downtown district, the City of Hanford identified in advance the types of commercial uses that serve as the economic anchors of district. Similarly, the local government identified department stores as the commercial anchor of the PC district, and ordered the types and scope of

---

[29] 159 P.3d 33 (Cal. 2007).

[30] Ibid. at 35, 39–40.

[31] Ibid. at 41–42.

commercial land uses within the district.[32] Therefore, the zoning ordinance did reflect a broad-based policy, not one merely tailored to protect private revenue streams of specific stores. For example, the Hanford zoning ordinance did nothing to limit the entry of new furniture stores in the downtown district or new department stores in the PC district. It did not limit the number of competitors, instead regulating their spatial distribution. The *Hernandez* case exemplifies how an explicit consideration of market externalities may be normatively legitimate when it relies on a broad-based policy.

4 Judicial Review of Market-Based Zoning

The previous Section laid the foundation for identifying market externalities resulting from land use, and explaining how zoning and other regulatory decisions could account for dimensions of aggregate welfare, distribution, and second-hand off-site technological or fiscal externalities embedded in market externalities. While there may be room for debate about the analysis of potential market externalities and the respective conclusions in contexts such as the entry of commercial uses, renting out of investment property, or inclusionary zoning, the control of market externalities should be explicitly recognized as a legitimate basis for zoning power.

At the same time, the need to tie the level of judicial review to the breadth and scope of the local land use policy plays a prominent role in the context of market externalities. The distinction between legislative or broad-based policy and ad hoc or adjudicative decision-making goes beyond considerations of rule of law, democratic accountability, and the need for occasional flexibility that regularly implicate land use law and policy (Fennell & Peñalver, 2014; Biber & Ruhl, 2014). I argue that the need to have a citywide, or at least an industry-wide, analysis prior to regulation touches on the very foundations of identifying the existence of a market externality and of normatively justifying the control over such potential effects through zoning rules.

From an economic perspective, a market externality is a process in which a certain market-equilibrium undergoes a change through the price system. This means that in most cases, a single development will not generate any type of market externality, but it might contribute to such a change in conjunction with other contemporaneous projects, resulting in a critical mass that creates a new equilibrium. When this is the case, identifying a market externality, or designing the adequate regulatory response (whether through a limit on land use, quota setting or a fee system), needs to be completed within a broader picture of the changing landscape of the city.

Indeed, there may be cases in which a single development could generate a market externality. This would be so especially in the case of a big-box retailer, such as a Wal-Mart Supercenter. Here too, however, a market analysis would require a broad

[32] Ibid. at 45–46.

analysis of the entire array of affected businesses, and more generally, of the policy choice between downtown business districts and spread-out retailers. An economic analysis based on agglomeration effects, or even on distributive concerns, would make little sense without a general policy on retail. These settings are therefore materially different from purely anticompetitive motives, such as when a single grocery store objects to a variance to set up a new grocery store on the other side of the street—with no discernible broader effects.

From a legal perspective, the generation of a market externality should be considered a blameless conduct, with no clear division between a wrongdoer and a victim. This is unlike some cases of environmental externalities, in which the normative basis of regulation lies in identifying a party who creates a conflict (even if such an action is not proscribed as a nuisance or another private law wrong), or of a fiscal externality, in which new public expenses must be incurred. As a matter of policy, individuals and firms should be encouraged to act in the market, promote competition and innovation, and otherwise stimulate the economy. There are cases in which considerations of agglomeration effects, distribution, or the possibility of second-hand externalities may justify the regulation of land uses intended for such an activity. However, these limits are not based on an initial normative judgment about the wrongful nature of the activity.

In contrast, no individual party can be viewed as legally entitled to block such an economic activity because this would infringe a legally recognized right or immunity from a change to the status-quo. A retailer has no vested right not to have competition around it, or to be compensated for such competition. A homeowner has no individual entitlement to prevent others from investing in real estate in his or her neighborhood. The justification for regulation lies in a general evaluation of the effects of a change to the market-equilibrium. As such, its legal validation must be based on a broad policy.

These observations do not preclude the possibility that in some cases, the regulation of a market externality must go beyond fixed formulas to provide a proper solution. The physical location of a big-box store, the type of products it is selling, and the composition of preexisting businesses may change across different scenarios, and would accordingly affect the identification of the market externality and the measures of control. This type of required flexibility should not be equated, however, with ad hoc decision-making, which attempts both to identify the problem and to cure it solely on a case-specific basis.

Conversely, in the case of technological, environmental or fiscal externalities, there could be cases in which an ad hoc analysis would be problematic, but at the least, it would be based on some initial normative baseline that identifies the cause of the externality and its anticipated consequences. The *Nollan/Dolan* framework, which requires localities that make ad hoc land use decisions to illustrate an "essential nexus" and "rough proportionality" between the development and its adverse consequences, inherently assumes that such an analysis of the cause and the cure can be made on an individual basis. In the case of a market externality, this assumption does not work. When a market externality is concerned, the "substantial relation" or "reasonable relationship" tests, while generally more lenient, may prove the only feasible way for courts to address the legal validity of zoning mechanisms intended to address market externalities. Such a legal standard provides relief to the local government by releasing it from having to identify a market externality that can be attributed to a specific project. At the same time, this standard also places a burden of persuasion on the local government. The city must demonstrate that the zoning rationale conforms to its broad policy, and would be applied elsewhere in the city.

Finally, one should consider the role of zoning decisions, and the legal standard that should apply to their review, when such decisions seek to focus on the generation of positive market externalities, rather than merely on preventing or mitigating negative market externalities resulting from new development.

The discussion of positive market externalities requires an even more manifested differentiation between private law entitlements and the legitimacy of land use regulation than is the case with adverse market externalities. The law of restitution usually does not entitle a benefactor to require payment or another kind of compensation from beneficiaries-in-fact, including when a developer carries out a project that provides unsolicited positive externalities.[33] A neighbor cannot be held liable for a self-serving activity by another landowner that incidentally improves the neighbor's land, even when the monetary value of the benefit is easily measured.[34] This principle also applies when the benefit stems directly from a specific land use regulation, such as when a developer is required, as a condition for approving his or her subdivision map, to construct an additional road to ensure that a neighboring landlocked property gain access to the nearest thoroughfare.[35]

The reasons for private law's reluctance to require beneficiaries to contribute to the internalization of positive externalities lie in considerations of autonomy and preference for pre-activity agreements, especially if the activity is sufficiently profitable for its doer, so that the "free riding" by the beneficiary will not undermine it altogether (Dagan, 2004). Authors have also pointed to other dimensions of asymmetry between benefits and harms, including the nature of scope of the potential effects in the absence of private law rules (Porat, 2009).

Yet regardless of the arguments against restitution in the private law context, zoning and other types of land use regulation are entitled to take into account the positive externalities that a proposed project may entail, and should aim to maximize such social benefits in order to promote the local "general welfare."[36]

Consider the following hypothetical: A city wants to introduce more retail activity within its jurisdiction. For this purpose, the city considers rezoning one of two

---

[33] See Green Tree Estates v. Furstenberg, 124 N.W.2d 90 (Wis. 1963) (holding that a developer was not entitled to recover from a neighbor for voluntary construction of street improvement, curbs, and gutters).

[34] See Ulmer v. Farnsworth, 15 A. 65 (Me. 1888) (rejecting the plaintiffs' claim for recovery after their pumping of water from their own quarry unavoidably drained water from the defendant's quarry).

[35] See Dinosaur Dev., Inc. v. White, 265 Cal. Rptr. 525, 526 (Cal. Ct. App. 1989) (rejecting the restitution-based claim of a developer against his neighbor under such circumstances).

[36] Referring to the underlying rationale of promoting the "general welfare" through the zoning power, articulated in Village of Euclid, 272 U.S. 365 at 388.

agricultural or currently undeveloped areas located in different parts of the city for commercial use. After a careful study, it concludes that, all else being equal, rezoning Area A would generate more positive market externalities for adjacent businesses and households, as compared with Area B, because of geographic and other considerations. Assume further that the city concludes that rezoning both areas simultaneously would result in excess commercial development, which could end in a massive closing down of businesses. A decision to approve the rezoning of area A, based on the analysis of such positive market externalities, should be considered legally valid. This would be so even if such a decision stands to benefit the current landowners of Area A over those of Area B, provided that retail developers could purchase land in Area A.

The more difficult issue is how to balance positive market externalities with the developer's self-interests, if these two components are not perfectly aligned. The municipality may have to offer developer incentives to ensure optimal land use. Consider again the city's hypothetical case. Assume now that the same developer owns both Area A and Area B in their entirety. The developer would actually prefer to develop Area B, because it is geographically closer than Area A to the seaport through which the developer imports its retail products, meaning that the developer would save on transportation costs if Area B is developed. Assume further that the sum of the developer's savings on transportation costs in Area B is smaller than the difference in positive market externalities in favor of Area A. However, because the developer cannot internalize the positive market externalities it is generating (assume that such externalities are not reciprocal), it will prefer to rezone Area B over Area A. What the city could do in such a case, for example, is to offer the developer a density bonus for developing Area A.

This decision should be anchored in a broad policy, by which the city incentivizes developers that generate positive market externalities. If the societal costs, including environmental costs resulting from increased density, do not outweigh the overall benefits from rezoning Area A over Area B, such a zoning decision should be considered both economically sensible and legally valid. Localities should accordingly extend explicit considerations of market externalities to facilitate positive externalities, beyond controlling against negative ones. Such a move would further aid in unveiling market externalities as the missing link in the evolution of zoning.

References

Been, V. (1991). "Exit" as a constraint on land use exactions: Rethinking the unconstitutional conditions doctrine. *Columbia Law Review, 91*, 473–545.

Benmelech, E., Bergman, N., Milanez, A., & Mukharlyamov, V. (2014). The agglomeration of bankruptcy, NBER working paper No. 20254. Retrieved February 23, 2017, from http://www.nber.org/papers/w20254

Biber, E., & Ruhl, J. B. (2014). The permit power revisited: The theory and practice of regulatory permits in the administrative state. *Duke Law Journal, 64*, 133–234.

Calabresi, G., & Melamed, A. D. (1972). Property rules, liability rules, and inalienability: One view of the Cathedral. *Harvard Law Review, 85*, 1089–1128.
Coase, R. H. (1960). The problem of social cost. *Journal of Law and Economics, 3*, 1–44.
Dagan, H. (2004). *The law and ethics of restitution*. Cambridge: Cambridge University Press.
Dari-Mattiacci, G. (2009). Negative liability. *Journal of Legal Studies, 38*, 21–60.
Ellickson, R. C. (1973). Alternatives to zoning: Covenants, nuisance rules, and fines as land use controls. *University of Chicago Law Review, 40*, 681–781.
Ellickson, R. C., Been, V. L., Hills, R. M., & Serkin, C. (2013). *Land use controls: Cases and materials* (4th ed.). New York: Wolters Kluwer.
Epstein, R. A. (2007). On Wal-Mart: Doing good by doing nothing. *Connecticut Law Review, 39*, 1287–1306.
Faulk, D. (2006). The process and practice of downtown revitalization. *Review of Policy Research, 23*, 625–645.
Fennell, L. A. (2009). *The unbounded home: Property values beyond property lines*. New Haven: Yale University Press.
Fennell, L. A., & Peñalver, E. M. (2014). Exactions creep. *Supreme Court Review, 2013*, 287–358.
Fischel, W. A. (2015). *Zoning rules: The economics of land use regulation*. Cambridge, MA: Lincoln Institute of Land Policy.
Fischler, R. (1998). The metropolitan dimension of early zoning: Revisiting the 1916 New York City ordinance. *Journal of American Planning Association, 64*(2), 170–188.
Glaeser, E. L., Gyourko, J., & Saks, R. E. (2005). Why have housing prices gone up? *American Economic Review, 95*(2), 329–333.
Goldenberg, S. (2015, July 31). *De Blasio plan would link affordable housing, rezoning*. Politico.
Haunshek, E. A., & Quigley, J. M. (1990). Commercial land use regulation and local government finance. *American Economic Review Papers and Proceedings, 80*(2), 176–180.
Holcombe, R. G., & Sobel, R. S. (2001). Public policy toward pecuniary externalities. *Public Finance Review, 29*, 304–325.
HUD (United States Department of Housing and Urban Development). (2011). Moving to opportunity for fair housing demonstration program: Final impacts evaluation. Retrieved February 23, 2017, from http://www.huduser.org/publications/pdf/MTOFHD_fullreport_v2.pdf
HUD (United States Department of Housing and Urban Development). (2013). Evidence matters: Inclusionary zoning and mixed-income developments. Retrieved February 23, 2017, from http://www.huduser.org/portal/periodicals/em/spring13/highlight3.html
Krugman, P. (1991). Increasing returns and economic geography. *The Journal of Political Economy, 99*, 483–499.
Laffont, J. J. (2008). Externalities. In S. N. Durlauf & L. E. Blume (Eds.), *The new Palgrave dictionary of economics* (2nd ed.). New York: Palgrave-Macmillan.
Lehavi, A. (2006). Intergovernmental liability rules. *Virginia Law Review, 92*, 929–989.
Martin, R., & Sunley, P. (1996). Paul Krugman's geographical economics and its implications for regional development theory: A critical assessment. *Economic Geography, 72*, 259–292.
Neumark, D., Zhang, J., & Ciccarella, S. (2008). The effects of Wal-Mart on local labor markets. *Journal of Urban Economics, 63*, 405–430.
O'Flaherty, B. (2005). *City economics*. Cambridge, MA: Harvard University Press.
O'Sullivan, A. (2009). *Urban economics* (7th ed.). New York: McGraw-Hill.
Pigou, A. C. (1932). *The economics of welfare* (4th ed.). London: Macmillan.
Porat, A. (2009). Private production of public goods: Liability for unrequested benefits. *Michigan Law Review, 108*, 189–227.
Quigley, J. M., & Raphael, S. (2005). Regulation and the high cost of housing in California. *American Economic Review Papers and Proceedings, 95*(2), 323–328.
Schwartz, J. (1997). Prisoners of proposition 13: Sales taxes, property taxes, and the fiscalization of municipal land use decisions. *Southern California Law Review, 71*, 183–217.

Shoag, D., & Veuger, S. (2015). Shops and the city: Evidence on local externalities and local government policy from big-box bankruptcies. Retrieved February 23, 2017, from http://scholar.harvard.edu/shoag/publications/shops-and-cityevidence-local-externalities-and-local-government-policy-big

Sun, L. G., & Daniels, B. (2014). Mirrored externalities. *Notre Dame Law Review, 90*, 135–186.

United States Census Bureau. (2012). Census of governments.. http://www.census.gov/govs/cog/. Accessed Feb. 23, 2017.

Whitten, R. H. (1917). The building zone plan of New York city. *National Municipal Review, 4*(3), 325–336.

Willis, C. (1995). *Form follows finance: Skyscrapers and skylines in New York and Chicago*. Princeton, NJ: Princeton Architectural Press.

Cases

California Building Industry Association v. City of San Jose 351 P.3d 974. (Cal. 2015).

Dinosaur Dev., Inc. v. White, 265 Cal. Rptr. 525, 526. (Cal. Ct. App. 1989).

Dolan v. City of Tigard 512 U.S. 374. (1994).

Green Tree Estates v. Furstenberg, 124 N.W.2d 90. (Wis. 1963).

Island Silver & Sp2ice, Inc. v. Islamorada, 542 F.3d 844. (11th Cir. 2008).

Koontz v. St. Johns Water Management District, 133 S. Ct. 2586. (2013).

Mugler v. Kansas, 123 U.S. 623. (1887).

Nollan v. California Coastal Commission, 483 U.S. 825. (1987).

Penn Central Transportation Co. v. City of New York, 438 U.S. 104. (1978).

Ulmer v. Farnsworth, 15 A. 65. (Me. 1888).

Village of Belle Terre v. Boraas 416 U.S. 1. (1974).

Village of Euclid v. Ambler Realty Co., 272 U.S. 365, 388. (1926).