CLUSTER DEVELOPMENT LAW OFFERS NEW OPPORTUNITIES FOR FLEXIBLE PLANNED DEVELOPMENT

By Guliet D. Hirsch, Esq., Archer & Greiner, P.C.

On August 7, 2013, Governor Christie signed into law a bill implementing numerous changes to the Municipal Land Use Law with the stated purpose of:

> *Enabling municipalities the flexibility to offer alternatives to traditional development through the use of equitable and effective planning tools, including clustering, transferring development rights and lot size averaging in order to concentrate development in areas where growth can best be accommodated and maximized while preserving agricultural lands, open space and historic sites.*
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> *N.J.S.A. 40:55D-2(p).*

The bill was promoted by New Jersey Future and supported by a diverse coalition.

Planned Development in New Jersey

The cluster development bill is the latest in a long history of planned development innovations. In 1967, the Municipal Planned Unit Development Act (P.L. 1967, c.61) was enacted in large part to respond to the call by University of Pennsylvania Professor Krasnowiecki for land use tools to encourage creativity and flexibility in development patterns. The Municipal Planned Unit Development Act encouraged municipalities to provide relief from conventional zoning by mutual agreement between the property owner and the board, including flexible provisions to allow greater density in one section in return for an offset in another section or the preservation of open space. It also created a first stage approval, known as "tentative approval" for planned developments, allowing full scale engineering to occur at the later final approval stage.

The Municipal Land Use Law, effective 1976, continued the State's tradition of supporting planned development options. The law created a series of planned development categories, including residential clusters, planned unit development or "PUD", and mixed uses of residential clusters and commercial or industrial uses. Zoning and subdivision ordinances were permitted to contain standards encouraging and promoting flexibility and economy in layout and design, N.J.S.A. 40:55D-39, -65; provisions authorizing a first stage concept approval (general development plan approval), N.J.S.A. 40:55D-45.1 to -45.8; and provisions governing the amount, location and methods for preserving common open space within the development, N.J.S.A. 40:55D-43.

New Cluster Development Bill

The recently passed cluster development bill, P.L. 2013, c. 106 (August 7, 2013), expands the options for flexible planned development. The new options are intended to allow municipalities to use clustering techniques, either through planned development ordinances or other provisions of the zoning ordinance, to encourage smaller scale projects providing for both cluster development and land preservation of agricultural, historic or open space land. In order to take advantage of the new cluster approach, municipalities will need to adopt a land use plan element addressing cluster development along with implementing zoning. Among the innovations of the new law are:

- Nonresidential development may also be clustered;
- Greater density may be provided in return for common open space, public open space or permanent preservation of historic or agricultural land;
- Cluster development should not be mandatory, but rather should be designed to foster mutual agreement between the applicant and the board on density and land preservation;
- Previously questioned zoning techniques are now expressly authorized, including the provision of bonus density or intensity; smaller scale cluster development; minimum and/or maximum lot sizes; lot size averaging; minimum improvable lot area; and minimum and/or maximum floor areas;
- Preservation restrictions are described.

The Next Steps

Implementing the Legislature's goals in the Cluster Development Act will require municipalities to be open to options which provide greater flexibility and less mandates for subdivision and site plans. It will also require the State to consider how reasonable densities in cluster developments can be achieved given the overriding concern about sewage disposal. Vacant land within approved sewer service areas is becoming rare, so cluster development may have to be served by septic systems. Current DEP standards for septic system density are dictating large lots, making cluster development densities unlikely without further innovations. The approach taken in the Pinelands Area has been to implement a pilot program to test advance septic system technologies, followed by DEP

Continued on Page 8

VALUING COMMERCIAL PROPERTY

By Dave Bossart, SCGREA, CCRA, CTA

If you are interested in investing in a commercial property purchase, there are three distinct questions to ask yourself: "What is this property worth?" "How much can I pay?" and "What can I get this property for?" All of those questions need answers before you put in an offer to purchase a commercial property.

How an investor chooses to value a property can depend on the size of the property or the sophistication of the purchaser. As an appraiser, I rely on the simple methods, both because my clients are new to commercial investing and because they are looking at small properties. But simple doesn't mean less reliable or less accurate when it comes to commercial valuation. Essentially, there are three ways to value a commercial property:

1. Direct Comparison Approach
2. Cost Approach
3. Income Approach (which includes the DCF method and the Capitalization Method).

The Direct Comparison Approach uses the recent sale details of similar properties (similar in size, location and if possible, tenants) as comparables. This method is quite common, and is often used in combination with the Income Approach.

The Cost Approach, also called the replacement cost approach, is not as common. And it's just what it sounds like; determining a value for what it would cost to replace the property: land plus building.

The third and most common way of valuing commercial real estate is using **The Income Approach**. There are two commonly used income approaches to value a property. The simpler way is the **Capitalization Rate Method**. Capitalization Rate, more commonly called the "Cap Rate," is a ratio, usually expressed in a percent that is calculated by dividing the Net Operating Income (NOI) into the Price of the Property. The cap rate method of valuing a property is where you determine what a reasonable cap rate is for the subject property by comparing it to other property sales; and then dividing that rate into the NOI for the property. It is equal to income minus vacancy minus operating expenses. Or, you could figure out the asking cap rate of the property by dividing the NOI by the asking price. It basically represents to the investor the return OF and the return ON their investment.

By way of example, if a property has leases in place that will bring in, after expenses (but not including financing) an NOI of $10,000 in the next year and comparable properties sell for cap rates of 6% then you can expect your property to be worth approximately $166,666 ($10,000/.06 = $166,666). Or, said another way, if the asking price of a property is $166,666, and its NOI is estimated at $10,000 for the next year, the asking cap rate is approximately 6%.

Where this gets tricky is when properties are vacant, or where the leases are set to expire in the upcoming year and are either higher or lower than the area market rent. This is often when you are forced to make some assumptions; which is a subject in itself for another article. The other income method is the **Discounted Cash Flow (DCF) method**. The DCF method is often used in valuing large properties like downtown office buildings or property portfolios. It is not simple, and it is a bit subjective. Multiple year cash flow projections, assumptions about lease rates and property improvements and expense projections are used to calculate what the property is worth today. Basically, you figure out all of the cash that will be paid out and all of the cash that will be brought in on a monthly basis over a specific period of time (usually the time you plan to hold the building for.) Then you determine what those future cash flows are worth today. There are computer programs like Argus Software that help in these types of valuations because there are many variables and many calculations involved.

For the small investor client, using a combination of comparable property sales and income valuation using cap rates will provide a reliable valuation. The real issue is convincing the seller that they should sell based on today's income and today's comparable properties. In the case of a mixed use commercial building we just tried to buy, the seller was pricing their property based on assumptions that leases will renew in the next six months at substantially higher rates and that the area of the property will continue to improve making the property more desirable.

Commercial property investment is not as reliant upon the property appreciating as is residential property. These clients buy properties today because the property will put more money in their pocket each month then it takes out, and the property fits within our investing goals.

Continued on Page 10

CLUSTER DEVELOPMENT LAW

Continued from page 4

issuance of a General Permit for the approved technologies (Permit No. 02-3487-4SG, issued 1/29/13). A similar approach is needed for the rest of the State to make cluster development a viable option.

Disclaimer: This article is for general information only and is not intended as legal advice or counsel.

[1] Krasnowiecki, Planned Unit Development Unit: A Challenge to Established Theory and Practice of Land Use Control, 114 U.Pa. L. Rev. 47 (1965).

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