

# From Theory to Practice: Institutional Insights into Inclusionary Zoning

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## ABSTRACT

Inclusionary zoning (IZ) links development approvals to affordable housing requirements and is an increasingly utilized policy tool globally. This literature review examines opportunities and prerequisites for implementing IZ in Malaysia's urban housing context through an institutional analysis lens. The paper's methodology involves a qualitative synthesis of academic scholarship from planning, policy, economics and law to develop a conceptual framework grounded in theory and comparative evidence. Analysis focuses on aligning IZ policy options with Malaysia's multi-tiered governance environment which poses particular challenges but allows localized piloting. After reviewing the theoretical underpinnings, global cases and core policy design considerations, an incremental approach is recommended beginning with voluntary incentives. This builds experience to progress eventually to broader mandatory inclusion aligned with institutional capacities. IZ is situated within a broader affordable housing strategy given limitation as a stand-alone panacea. Tailored, modest initiatives can expand access without overburdening still-developing administrative systems. The review elucidates pragmatic steps to unlock IZ benefits in Malaysia through contexts-specific programs that judiciously harness market forces while adapting to institutional realities. The synthesized perspective informs policy-making and suggests future research directions to deepen understanding of implementing inclusionary models in Asian developing country contexts.

**Keywords:** Inclusionary Zoning, Affordable Housing, Planning

## INTRODUCTION

Malaysia faces pressing affordable housing challenges, with homeownership beyond reach for many lower and middle-income urban households despite robust market-rate development [13],[29],[33]. Inclusionary zoning (IZ) has emerged globally as a policy lever to expand affordable housing supply by leveraging private residential markets. IZ ties zoning approvals to requirements for below-market rate set-asides in new projects [6]. Well-designed and context-specific IZ policies have shown success in high-cost cities worldwide. IZ holds strong potential for addressing Malaysia's affordability gaps through mandates on private developers. However, effective IZ adoption depends on aligning policy features with local institutional capacities.

This paper examines prerequisites and pathways for implementing inclusionary zoning in Malaysia through an institutional policy analysis lens. The theoretical underpinnings of IZ in market failure and governance contexts are reviewed. Comparative cases from Asia and beyond demonstrate how institutional structures shape IZ approaches and outcomes. Malaysia's complex multi-tiered governance environment poses inherent constraints but also flexibility for localized pilot initiatives. Core components of IZ policy design are discussed, emphasizing economic feasibility, legal authority, administrative coordination and program calibration. Alternatives and limitations are considered, situating IZ as part of a broader affordable housing strategy.

The overall objective is to elucidate institutional opportunities and challenges for tailored IZ policies in Malaysia that leverage market forces while adapting to political and governance realities. Pragmatic recommendations are provided for phased implementation through modest voluntary programs toward more comprehensive mandatory inclusionary requirements as capacities strengthen over time. The paper aims to inform context-appropriate IZ approaches to expand affordable access without overburdening still-developing administrative systems.

## LITERATURE REVIEW

### Theoretical Underpinnings of IZ

Economic theory conceptualizes IZ as a supply-side intervention to harness private housing development to generate new below-market rate units [25]. By requiring affordable set-asides or in-lieu fees linked to market-rate development, IZ expands overall housing supply rather than just redistributing access [9]. This approach aligns with the idea that the unpriced positive external benefits of below-market rate units and mixed-income communities provide an economic rationale for IZ mandates on private developers [9]. In essence, IZ becomes a mechanism to correct market failures stemming from neighbourhood exclusion that restricts affordable housing supply in high-opportunity areas [25]. The policy thus aims to internalize these external welfare effects and promote more optimal social outcomes.

Political economy scholarship emphasizes that the feasibility and outcomes of IZ depend on the local institutional context. State powers to enable IZ, planning agency capacities, housing market conditions, and political dynamics shape whether IZ policies are adopted and how effective they are [5]. Within this framework, institutionalist theories provide a lens through which to analyze IZ. The diverse interests, incentives, and powers of actors in housing and land use systems determine IZ policy formation and impacts [5]. Moreover, institutional coordination issues, administrative capacities, and regulatory constraints create challenges for implementing IZ programs [22]. An institutional analysis thus illuminates the necessary conditions, frictions, and adaptations needed for IZ to work effectively given a jurisdiction's governance context.

IZ policies, rooted in economic theory and institutionalist perspectives, represent a comprehensive approach to addressing the complex issue of affordable housing. The interconnected nature of economic incentives, external benefits, and institutional structures underscores the need for a nuanced understanding of IZ's role in shaping housing markets and community development. In navigating the challenges of implementation, policymakers must consider both the economic rationale behind IZ mandates and the intricate web of institutional dynamics that influence their outcomes. By doing so, they can foster a more holistic and effective approach to promoting affordable housing within diverse urban landscapes.

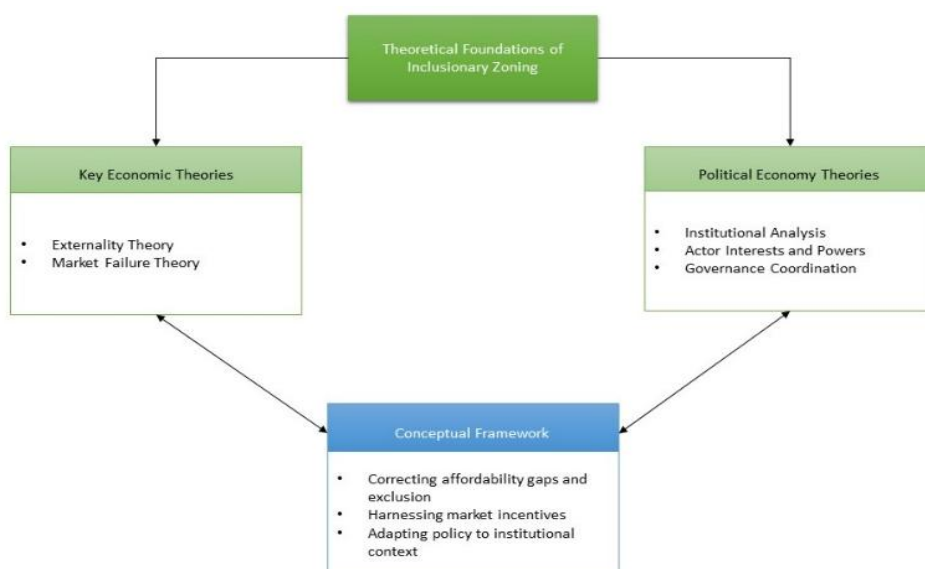


Figure 1: Theoretical Foundations of Inclusionary Zoning

Figure 1 shows the two main theoretical lenses of economics and political economy feeding into an overall conceptual framework for understanding and applying IZ. The economic theories focus on market failures and externalities that IZ aims to address. The political economy view looks at actor incentives and institutional contexts. The conceptual framework synthesizes these perspectives to show how IZ policies can leverage markets while requiring adaption to local governance conditions.

### **Global Evidence on Importance of Local Institutional Contexts**

Comparative research on IZ globally has underscored how local institutional variables determine IZ policy impacts [6]. Strong state enabling legislation with mandates, incentives, and cost offsets provide an essential foundation for successful municipal IZ programs in the US [22]. Moreover, the presence of robust state-level regulations not only sets the stage for IZ but also influences the effectiveness of municipal initiatives. Local planning agency capacities to design context-appropriate IZ policies, provide oversight, and coordinate with developers are also critical implementation factors. The interplay between state directives and local execution mechanisms emphasizes the need for a cohesive and well-coordinated approach to IZ. Local political support, housing market conditions, and land availability further enable the adoption and outcomes of IZ programs [25]. The intersection of political backing, market dynamics, and land resources underscores the multifaceted nature of IZ implementation. Experiences in other Asian countries likewise highlight the need to tailor IZ policies to local institutional contexts. For instance, Hong Kong's IZ approach utilizes strong public land leasing powers, while Japan's relies more on incentives due to weaker state powers [30].

While economic feasibility and broader housing market conditions influence IZ outcomes, research shows that local institutional structure is the most significant determinant of policy effectiveness [22]. Understanding the nuanced interplay between economic factors and institutional dynamics is crucial for shaping successful IZ policies. Studies of IZ programs across California found that strong public sector capacities were critical for successful adoption and implementation, often more so than private real estate dynamics [5]. This highlights the paramount importance of governmental capabilities in driving the success of IZ initiatives. Municipalities with staff expertise to design context-sensitive IZ policies, provide technical assistance, and foster public-private collaboration achieved better outcomes in terms of units produced and income integration [25]. The collaborative synergy between public entities and private developers emerges as a crucial element in the overall effectiveness of IZ programs. Recent comparative analysis of IZ in Massachusetts reaffirmed the key role of municipal administrative and regulatory powers in shaping the strength and impacts of policies [25],[28],[16].

International experience likewise highlights how enabling legislation, governance coordination, and political will make or break IZ policies. South Africa's inclusionary housing program depended on national regulatory changes to empower provinces and cities to enact mandatory schemes [13]. This underscores the ripple effects of policy decisions at the national level on the success of IZ at the local level. In Brazil, fragmentation between different levels of government was a main constraint, pointing to the needs for integrated policy and administration [21]. The challenges faced in Brazil emphasize the importance of a unified approach to policy implementation across various administrative tiers. Political leadership to champion, fund, and oversee IZ has also proven important across contexts from Colombia to India [22]. The role of political leadership emerges as a common thread in the successful execution of IZ policies, transcending geographical and cultural boundaries. Malaysia's complex institutional environment will similarly require aligning policy design with governance capabilities and coordination. The Malaysian case serves as a reminder that each locality must navigate its unique institutional landscape to effectively implement IZ and address affordable housing challenges.

### **Case Studies of Inclusionary Housing Approaches in Asia**

Asian countries provide useful examples of varied IZ policy designs adapted to local contexts as shown in Table 1. Singapore's required quotas for public housing integration depend on the city-state's extensive control of land [7]. In this vein, Singapore's approach exemplifies the direct correlation between governmental control over land resources and the successful implementation of IZ policies. Japan's voluntary approach utilizes incentives like tax abatements due to weaker mandating powers [12]. Japan's reliance on voluntary measures showcases the adaptability of IZ policies to accommodate varying levels of regulatory strength, emphasizing the role of incentives in the absence of strong mandates. India has piloted mandatory IZ linked to zoning permissions, with

states tailoring ordinances to needs and capacities [17]. The Indian model demonstrates the potential success of aligning IZ with zoning regulations, recognizing the importance of tailoring policies to the specific needs and capacities of different states. Provinces in China have implemented modified IZ requirements on a demonstration basis, enabled by recent housing reforms [31],[32]. The Chinese experience reflects a proactive response to housing reforms, indicating the dynamic nature of IZ policy evolution and the role of regulatory changes in shaping its implementation. While not extensively studied, early Asian experiences mirror global evidence on aligning IZ policies with institutional environments.

Table 1: Inclusionary Zoning Policy Approaches in Selected Asian Countries

Country	IZ Approach	Key Features
Singapore	Mandatory Quotas	<ul style="list-style-type: none"> <li>• Set percentages of units in new private developments</li> <li>• Enabled by extensive public control of land</li> </ul>
Japan	Voluntary Incentives	<ul style="list-style-type: none"> <li>• Tax abatements and density bonuses used rather than mandates</li> <li>• Due to limited state regulatory power over housing</li> </ul>
India	Mandatory Linkages	<ul style="list-style-type: none"> <li>• Tied to zoning approvals in some states/cities</li> <li>• Policy design adapted locally due to devolved powers</li> </ul>
China	Pilot Demonstrations	<ul style="list-style-type: none"> <li>• Required percentages tested in selected provinces</li> <li>• Part of recent housing reforms expanding local authority</li> </ul>

## METHODOLOGY

This paper utilizes a qualitative review of relevant literature on inclusionary zoning to conduct an institutional analysis of policy considerations for the Malaysian context. Published academic scholarship from the fields of urban planning, housing policy, economics, and law are reviewed to provide theoretical grounding and evidence-based insights. The literature review encompasses both global perspectives and Malaysia-specific research.

Key word searches for relevant literature were conducted using Google Scholar and academic databases. Search terms included “inclusionary zoning”, “inclusionary housing”, “affordable housing”, “Malaysia”, “institutions”, “governance”, and related phrases. Priority was given to recently published studies in leading journals. Literature was selected to provide diversity of geographic perspectives, methodologies, and disciplinary foundations.

## RESULTS & DISCUSSIONS

### The Institutional Landscape for Housing and Land Use Planning in Malaysia

In Malaysia, housing and land use planning powers are divided between federal, state, and local governments. The federal government provides overall policy direction but lacks direct IZ enabling authority [26]. Despite setting the overarching policy direction, the federal government's inability to directly enable IZ underlines the decentralized nature of housing governance. Most regulatory powers lie with state governments, including approving development plans and schemes [3],[4],[24]. However, states differ significantly in their planning capacities, and the lack of uniformity in their capabilities creates disparities in housing and land use strategies. Coordination across agencies can be challenging especially when dealing with varying levels of planning competence among different states. Local councils, positioned at the frontline, have limited discretionary powers and rely on standardized planning processes [11]. This standardization underscores the need for a more flexible and adaptive approach, especially in the context of IZ, within Malaysia's diverse urban landscape. The complex institutional environment poses constraints for IZ adoption, pointing to a need for incremental approaches aligned with existing governance capacities and structures.

The complex dynamic between federal, state, and local authorities in Malaysia creates coordination challenges that complicate housing and land use planning [18],[23]. The federal government has sought greater oversight of affordable housing through entities like the National Housing Department (NHD), but tensions remain over



jurisdictional authority [8],[20]. This tension highlights the ongoing struggle for regulatory control, emphasizing the need for clearer delineation of responsibilities to facilitate effective housing and land use planning. State governments hold principal powers over land and housing but vary enormously in their technical capacities, financial resources, and policy priorities [4],[24]. This variation calls for a tailored approach that recognizes and accommodates the diversity among states, acknowledging that a one-size-fits-all strategy may not be feasible. Local councils have minimal discretion and rely on approvals from higher levels [11]. The limited autonomy of local councils' points to the necessity of empowering them with more decision-making authority to enhance the adaptability of housing plans. Weak vertical and horizontal coordination between agencies at different tiers further hinders regulatory coherence [19], emphasizing the critical need for improved collaboration and communication to streamline housing and land use policies.

These institutional complexities have produced a fragmented housing planning framework. For instance, conflicting mandates and lack of coordination between ministries led to severe mismatches between housing supply and demand under the Five-Year Plans [2]. The historical context reveals the pitfalls of fragmented planning and calls for a more integrated and collaborative approach to prevent such mismatches in the future. Top-down target setting with little local input also weakened past public housing programs (NHD, 2011). This historical precedent underscores the importance of incorporating local perspectives and needs into the planning process to ensure the effectiveness of housing programs. Malaysia's institutional environment poses inherent challenges but also allows flexibility for innovative approaches like IZ tailored to specific state and local contexts. Recognizing the unique characteristics of Malaysia's institutional environment opens the door for creative solutions, emphasizing the potential for IZ to be a flexible and adaptable tool in addressing housing challenges within the country.

### **Fundamentals of a Well-designed Inclusionary Policy**

The design of an IZ policy is critical to its effectiveness within a given institutional context. Key provisions like incentives, affordability targets, and integration guidelines must be calibrated based on economic and financial feasibility [5]. Achieving the delicate balance between these provisions requires a nuanced understanding of the local housing market dynamics and economic conditions. Enforceable requirements need appropriate legal grounds, relying on state planning acts or housing legislation [6]. The legal foundation serves as the backbone of the policy, ensuring its legitimacy and effectiveness. Administration of IZ programs further depends on capable implementing agencies and coordination protocols. Building administrative capacity and establishing effective coordination mechanisms are crucial components in translating policy into action. Piloting IZ in Malaysia would require careful policy crafting attuned with the local institutional environment, with features like phased implementation, political acceptability, and administrative coordination.

International best practices point to key features of robust IZ policy design, but adapting programs to local contexts remains essential [6]. While drawing inspiration from global models, tailoring IZ policies to Malaysia's unique socio-economic and institutional landscape is imperative. Technical analyses to set feasible affordability targets and requirements calibrated to housing market conditions help create realistic, effective policies [25]. This analytical approach ensures that policy goals align with the practical realities of the Malaysian housing market. Sufficient cost offsets like density bonuses and fast-tracked permitting are needed to overcome developer resistance [5]. Addressing potential challenges from developers requires strategic planning that includes enticing incentives. Legal provisions should withstand potential court challenges through careful enabling legislation [15]. Ensuring legal resilience is crucial to prevent setbacks and legal disputes that could impede the successful implementation of IZ. Program guidelines must balance prescribed standards with flexibility for negotiation on a project-by-project basis [14]. Striking this balance is vital to accommodate the diverse nature of development projects and foster collaboration between policymakers and developers.

Malaysia's institutional constraints require an incremental approach to designing IZ policy, focused initially on voluntary, incentive-based programs or limited mandatory schemes. The gradual introduction allows policymakers to gauge the effectiveness of the policy within the existing institutional framework. Context-specific economic feasibility studies are imperative to inform pilot programs [6]. Rigorous economic analyses provide the necessary foundation to tailor IZ policies to Malaysia's specific economic conditions. Review processes allowing feedback from housing industry stakeholders could also increase buy-in. Incorporating

stakeholder perspectives enhances the inclusivity of the policy-making process and increases the likelihood of successful implementation. With demonstrated successes, more comprehensive mandatory IZ could be enacted – but would require careful policy crafting and coalition-building attuned to Malaysia’s governance capacities and political landscape. This phased approach ensures that policy changes are responsive to local dynamics and build upon proven success.

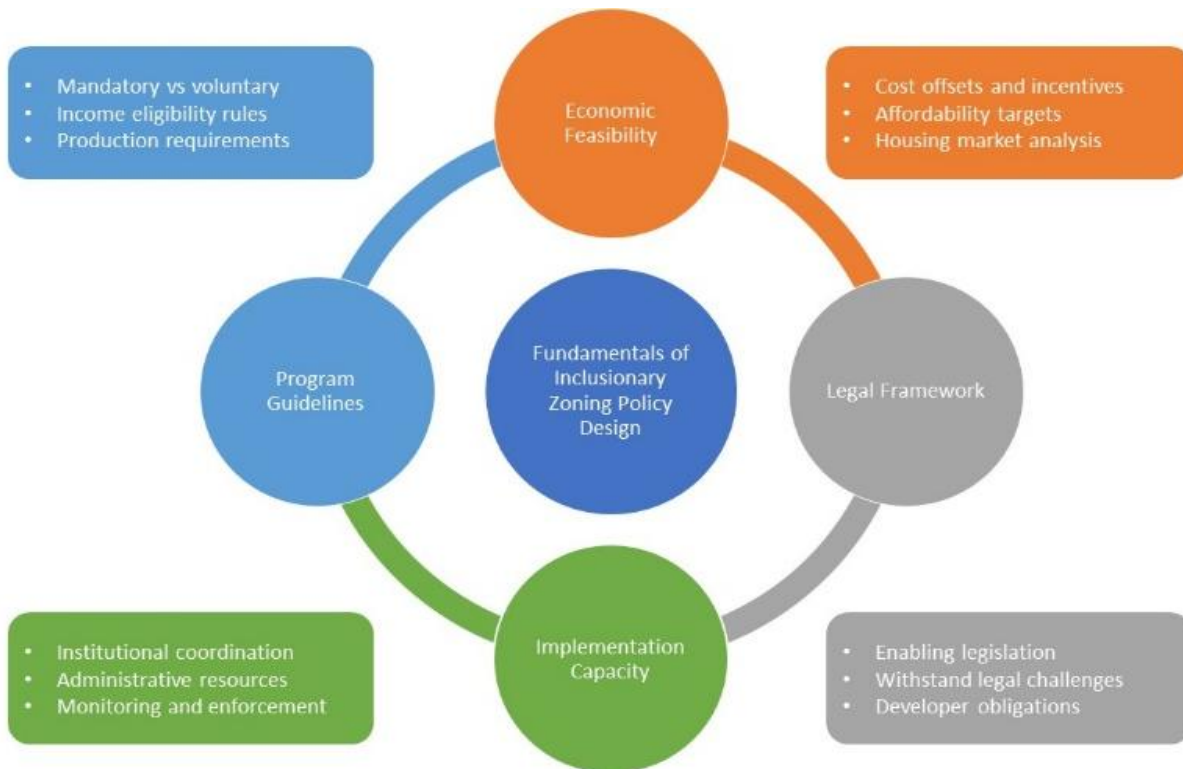


Figure 2: Fundamentals of Inclusionary Zoning Policy Design

The core components of an effective IZ policy design can be summarized across four interdependent dimensions, as shown in the Figure 2. Economic feasibility analysis, robust legal foundations, strong institutional capacity, and well-calibrated programmatic guidelines are all crucial in crafting policies tailored to local contexts. The interlinkages between these domains require careful calibration in IZ policy formation, balancing prescriptive standards with flexibility for negotiation and refinement over time. Malaysia’s institutional constraints call for modest initial policy designs focused on voluntary, incentive-based approaches to build experience and capacities to support more comprehensive mandatory inclusionary requirements.

## CONCLUSION

Inclusionary zoning offers a promising tool for expanding affordable housing in Malaysia, but adopting IZ requires aligning policy designs with the country’s institutional capacities and constraints. Malaysia’s complex governance environment calls for an incremental approach focused initially on voluntary, incentive-based programs. Economic feasibility analyses and review processes to inform pilot projects could facilitate implementation within current planning systems. As institutional coordination strengthens over time, more comprehensive mandatory IZ may become feasible. Institutional capacity-building and coordinated governance will remain critical in scaling up policies. IZ on its own cannot resolve all housing needs, underscoring integration into a broader strategy with complementary measures. With appropriately tailored and realistic policies, IZ can make a valuable contribution to affordable housing in Malaysia despite inherent institutional challenges.

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