GO Item 3
June 25, 2015
Worksession

MEMORANDUM

June 23, 2015

TO: Government Operations and Fiscal Policy Committee

FROM: Jeff Zyontz, Senior Legislative Analyst

SUBJECT: **Worksession:** Bill 8-15, Taxation – Development Impact Tax - Exemptions

Bill 8-15, Taxation – Development Impact Tax - Exemptions, Lead sponsor Council Vice-President Floreen; Co-sponsors - Councilmembers Riemer, Rice, Katz and Navarro, was introduced on February 3. Bill 8-15 would exempt the market-rate rental dwelling units in any development which consists of at least 25% affordable housing units from the transportation and school development impact taxes.[1]

This Bill is similar to Bill 39-11 as recommended by the Government Operations and Fiscal Policy Committee. On May 7, 2013, the Council considered Bill 39-11 with the recommended revisions and laid the bill on the table. Bill 39-11 expired without further action on December 1, 2014.

On March 3, 2015 the Council held a public hearing on Bill 8-15. The Montgomery Housing Partnership spoke in favor of the Bill (©19-20). In their view, the impact tax burden is a burden on all new housing but has the most negative effect on those projects that provide affordable housing. The Partnership encouraged the Council to expand Bill 8-15 to for-sale projects in addition to rental projects. The Council held another public hearing on May 5, 2015 in order to comply with noticing requirements. No one spoke at the Council's May 5 public hearing.

Fiscal impact

The Executive submitted a fiscal impact statement assuming that every rental project beyond approved development would all make themselves eligible for the exemption under Bill 8-15 by providing 25% affordable units. Based on this absolute worst case situation, the Executive estimated the potential for $48.6 million in lost revenue and a gain of 634 affordable units.[2]

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[1] Affordable units include MPDUs, and other units if the rent affordable to households earning less than 60% of the area median income, adjusted for family size for a minimum 15 year term;

[2] Worst case from the perspective of reduced impact fee revenue.

The exclusion of Bill 8-15 on projects in the development pipeline is significant. All of the projects that include those units will be excluded from the potential for fee relief. New projects would take 3 years to go from preliminary to the point where impact fees become due. For the next 3 years (FY 16 thru FY 19), the fiscal impact would be zero.

Staff used the perimeters of Bill 8-15 when it wrote the memorandum to Council on Bill 39-11 (attached). Staff estimated the annual amount of reduced fees would be $2.1 million per year starting 4 years after the date the bill is effective, assuming one building per year takes advantage of the exemption.

Both the 2013 staff analysis and the 2015 OMB fiscal impact statement were in the same ballpark on one point. The permit cost for each additional affordable unit will cost the County approximately $80,000 per unit.[3]

Issues

Bill 8-15 reflects all of the Committee's opinions from 2013. The issues discussed and resolved by the Committee were as follows:

Should the incentive for additional affordable housing be a tax credit or a specific grant?

A reduction of impact fees does not relieve the County from the obligation to provide infrastructure. Tax relief will ultimately require the burden of transportation and infrastructure to be bourn more by all tax payers and less by new development. To the extent that developers take advantage of Bill 8-15, it is like a tax expenditure except that it concerns a fee and not a tax.[4] Revenues are reduced by the amount of relief automatically and thereby giving an automatic subsidy to the project. The applicant need not pay the fee and then apply for a grant to get a refund.

Compared to a grant, a fee exemption shifts the financial burden in a less transparent and potentially uncontrollable manner. The fee exemption will cause the Council to write a bigger check for infrastructure using tax payer funds or raise the fee for all other non-exempt projects. A direct grant would cause the Council to write a check to a particular project using tax payer funds. The fee reduction does not require specific Council or agency action. Grant requests would have to be processed and approved.

If staff's assumption that only one project a year will provide more than 25% affordable units then grants are a clear option instead of a fee exemption. If the Council is concerned about the potential fiscal impact of Bill 8-15, the grants to refund impact fees would make the fiscal impact controllable.

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[3] The 2015 OMB study estimate the cost at $76,619 per additional affordable unit; in 2013, staff estimated that same cost to be $81,600 in Metro Station Policy Areas and $111,520 outside of those areas where multifamily construction is less likely.)

[4] Tax expenditures" are subsidies delivered through the tax code as deductions, exclusions, and other tax references. Tax expenditures reduce the amount of tax that households or corporations owe. To benefit from a tax expenditure, a taxpayer must undertake certain actions or meet certain criteria.

In 2013 the Committee recommended a fee exemption for highly affordable housing projects. Staff would recommend accomplishing the same results by grants. The Housing Initiative Fund (HIF) is already established to provide such grants. The HIF could always benefit from additional funding.

Should there be a dollar limit on the exemption?

The Executive's fiscal impact creates the fear of a substantial loss of funds available for school and transportation infrastructure. In 2013 the Committee's response to this concern was to reduce the scope of the exemption in other ways. The advantage of a dollar limit is that the revenue gap created by the exemption would be controlled by the Council and not be the decisions made by developers. There are already dollar limits on some tax credit programs such as historic preservation and energy conservation. In 2013, the Committee did not recommend a dollar limit.

Should pipeline projects be excluded?

Reducing the number of potential projects that may earn an exemption is a means of reducing the fiscal impact of Bill 8-15. There are more than 21,000 multifamily units in the pipeline.[5] Dropping those projects that have preliminary plan or site plan from the proposed exemption evolved from the following narrative:

> The intent of Bill 8-15 is to make the economics of affordable housing a little bit better. The fee relief would never fully make-up for lower rents. Projects that have paid for processing costs for preliminary plan or site plan approval do not need that extra boost.

In 2013 staff estimated that in addition to the approved pipeline, there was zoning capacity for 55,000 multi-family dwelling units. The new zoning code significantly increased that potential by allowing commercial floor area to be used for residential purposes. There is a large pool of potential beneficiaries of Bill 8-15 even when projects with preliminary plan or site plan approval are excluded.

Should publicly owned projects be excluded?

The Bill as introduced would bar publicly owned land or land previously owned by the public from being eligible for the fee exemption. The term publicly owned is much broader than County owned. It includes the County, the State, and the Federal government as these are all public entities. Publicly owned also includes all land titled to government agencies (Maryland-National Capital Park and Planning Commission, Washington Suburban Sanitary Commission, and Washington Metropolitan Area Transit Authority) and instrumentalities (Housing Opportunity Commission (HOC) and the Revenue Authority).

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[5] 21,439 units in mixed use projects - May 2015 Planning Staff Pipeline Report.

Publicly owned land is sometimes sold at discounts to affordable housing providers. It was the Committee's opinion in 2013, that such land be excluded from the exemption. In 2013, staff estimated that this exception to the exemption would affect 2,700 total multi-family dwelling units.

As noted, HOC is a public instrumentality. Bill 8-15 would bar HOC owned land from benefiting from the fee exemption.[6] The Bill's sponsor wants the Committee to consider allowing HOC to benefit from the fee exemption.[7]

In 2013 the Committee considered and rejected the idea of limiting the exception to the exemption to County owned land. That would be the narrowest exception to the impact fee exemption.

Should projects that are receiving zoning accommodation for additional affordable housing be excluded from?

The zoning code allows greater flexibility when a development provides Moderately Priced Dwelling Units (MPDUs). The MPDU provisions for lower density residential zones allow a greater variety of unit types, small sized developments, and smaller lot sizes. As lower density development commands higher rents, it is not expected that this type of development would provide more than 25% affordable dwelling units under any circumstances.

The higher density zones allow floor area bonus density for the provision of public benefits. MPDUs above the required 12.5% can be one of the public benefits at the option of the developer. Some zones allow greater density and greater height for the provision of affordable housing.[8] As introduced, the provision for additional affordable units may only be exempt from impact fees if the project does not get bonus density for the same attribute.

Should 25% affordable dwelling units be the trigger point for the exemption?

In 2013 the Committee consulted with HOC who claimed that 25% was that maximum that some "mission driven" affordable housing providers could accommodate. The Department of Housing and Community Affairs (DHCA) negotiates for 30% affordable units when it has the opportunity to sell publicly owned land. Increasing the percentage of affordable units would

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[6] HOC is flexible on ownership. In some instances HOC retains ownership of projects, sells ownership, or sells part of the ownership of projects.

[7] Bill 8-15 would be revised in part to read:

> The tax under this Article must not be imposed on:
>
> > any non-exempt rental dwelling unit in a development in which at least 25% of the dwelling units are exempt under paragraph (1), (2), (3), or (4), or any combination of them, if:
> >
> > (A) the development is located on privately owned land, land owned by HOC; or
> >
> > (B) the land that was privately-owned or HOC owned when the development was proposed; and....

[8] CR and CRT zoned properties with a "T" may exceed the otherwise maximum height and density of the zone if more than 12.5% MPDUs are provided or workforce housing is provided. Section 59.4.5.2.C

decrease the universe of applicants who may wish to take advantage of the fee exemption. The Committee retained the 25% affordable unit trigger.

Should there be a sunset provision to the exemption?

The Committee rejected the inclusion of a sunset provision in 2013. The Council is perfectly capable of repealing or amending the Bill's provision after it is put into practice; however, a sunset provision would **require** the Council to judge the merits of the exception at a later date.

This packet contains:

GO Memo 6-25-15

Bill No. 8-15
Concerning: Taxation - Development Impact Tax - Exemptions
Revised: 1-20-15 Draft No. 1
Introduced: February 3, 2015
Expires: August 3, 2016
Enacted: ______
Executive: ______
Effective: ______
Sunset Date: None
Ch. ____, Laws of Mont. Co. ______

COUNTY COUNCIL
FOR MONTGOMERY COUNTY, MARYLAND

Lead Sponsor: Council Vice-President Floreen;
Co-Sponsors Councilmembers Riemer, Rice, Katz and Navarro

AN ACT to:
(1) exempt certain housing units from certain development impact taxes; and
(2) generally amend the law governing development impact taxes.

By amending
Montgomery County Code
Chapter 52, Taxation
Sections 52-49 and 52-89

Boldface	*Heading or defined term.*
Underlining	*Added to existing law by original bill.*
[Single boldface brackets**]**	*Deleted from existing law by original bill.*
Double underlining	*Added by amendment.*
[[Double boldface brackets**]]**	*Deleted from existing law or the bill by amendment.*
* * *	*Existing law unaffected by bill.*

The County Council for Montgomery County, Maryland approves the following Act:

Section 1. Sections 52-49 and 52-89 are amended as follows:

52-49. Imposition and applicability of development impact taxes.

* * *

(g) A development impact tax must not be imposed on:

(1) any Moderately Priced Dwelling Unit built under Chapter 25A or any similar program enacted by either Gaithersburg or Rockville;

(2) any other dwelling unit built under a government regulation or binding agreement that limits for at least 15 years the price or rent charged for the unit in order to make the unit affordable to households earning less than 60% of the area median income, adjusted for family size;

(3) any Personal Living Quarters unit built under Sec. 59-A-6.15, which meets the price or rent eligibility standards for a moderately priced dwelling unit under Chapter 25A;

(4) any dwelling unit in an Opportunity Housing Project built under Sections 56-28 through 56-32, which meets the price or rent eligibility standards for a moderately priced dwelling unit under Chapter 25A;

(5) any non-exempt rental dwelling unit in a development in which at least 25% of the dwelling units are exempt under paragraph (1), (2), (3), or (4), or any combination of them, if:

(A) the development is not located on publicly-owned land or land that was publicly-owned when the development was proposed; and

(B) the development has not received other benefits under Chapter 59 because the development includes more than the minimum required affordable housing; and

[(5)] (6) any development located in an enterprise zone designated by the State or in an area previously designated as an enterprise zone.

* * *

52-89. Imposition and applicability of tax.

* * *

(c) The tax under this Article must not be imposed on:

(1) any Moderately Priced Dwelling Unit built under Chapter 25A or any similar program enacted by either Gaithersburg or Rockville;

(2) any other dwelling unit built under a government regulation or binding agreement that limits for at least 15 years the price or rent charged for the unit in order to make the unit affordable to households earning less than 60% of the area median income, adjusted for family size;

(3) any Personal Living Quarters unit built under Sec. 59-A-6.15, which meets the price or rent eligibility standards for a moderately priced dwelling unit under Chapter 25A;

(4) any dwelling unit in an Opportunity Housing Project built under Sections 56-28 through 56-32, which meets the price or rent eligibility standards for a moderately priced dwelling unit under Chapter 25A;

(5) any non-exempt rental dwelling unit in a development in which at least 25% of the dwelling units are exempt under paragraph (1), (2), (3), or (4), or any combination of them, if:

(A) the development is not located on publicly-owned land or land that was publicly-owned when the development was proposed; and

(B) the development has not received other benefits under Chapter 59 because the development includes more than the minimum required affordable housing; and

[(5)] (6) any development located in an enterprise zone designated by the State or in an area previously designated as an enterprise zone.

* * *

Section 2. Applicability. County Code Section 52-49(g)(5) and Section 52-89(c)(5), both inserted by Section 1 of this Act, do not apply to any development which received preliminary subdivision plan approval or site plan approval (or a similar approval in a municipality) before this Act took effect.

Approved:

George Leventhal, President, County Council Date

Approved:

Isiah Leggett, County Executive Date

This is a correct copy of Council action.

Linda M. Lauer, Clerk of the Council Date

LEGISLATIVE REQUEST REPORT

Bill 8-15
Taxation – Development Impact Tax - Exemptions

DESCRIPTION:	Exempts the market-rate rental dwelling units in any development which consists of at least 25% affordable housing units from the transportation and school development impact taxes.
PROBLEM:	Need to encourage provision of affordable housing.
GOALS AND OBJECTIVES:	To create further incentives to increase the share of low- and moderate-income housing in new developments
COORDINATION:	Department of Permitting Services, Department of Housing and Community Affairs, Planning Board
FISCAL IMPACT:	To be requested.
ECONOMIC IMPACT:	To be requested.
EVALUATION:	To be requested.
EXPERIENCE ELSEWHERE:	To be researched.
SOURCE OF INFORMATION:	Robert H. Drummer, Senior Legislative Attorney, 240-777-7895
APPLICATION WITHIN MUNICIPALITIES:	Impact taxes apply County-wide.
PENALTIES:	Not applicable.

B8-15

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ROCKVILLE, MARYLAND

MEMORANDUM

March 31 , 2015

TO: George Leventhal, President, County Council

FROM: Jennifer A. Hughes, Director, Office of Management and Budget
Joseph F. Beach, Director, Department of Finance

SUBJECT: FEIS for Bill 8-15, Taxation – Development Impact Tax - Exemptions

Please find attached the fiscal and economic impact statements for the above-referenced legislation.

JAH:fz

cc: Bonnie Kirkland, Assistant Chief Administrative Officer
Lisa Austin, Offices of the County Executive
Joy Nurmi, Special Assistant to the County Executive
Patrick Lacefield, Director, Public Information Office
Joseph F. Beach, Director, Department of Finance
Diane Jones, Department of Permitting Services
David Platt, Department of Finance
Alex Espinosa, Office of Management and Budget
Dennis Hetman, Office of Management and Budget
Felicia Zhang, Office of Management and Budget
Naeem Mia, Office of Management and Budget

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Fiscal Impact Statement
Council Bill 8-15 Taxation – Development Impact Tax - Exemptions

1. **Legislative Summary.**

   Bill 8-15 would exempt the rental market-rate dwelling units in any housing development which consists of at least 25% affordable housing units from the transportation and school development impact taxes they would otherwise have to pay.

2. **An estimate of changes in County revenues and expenditures regardless of whether the revenues or expenditures are assumed in the recommended or approved budget. Includes source of information, assumptions, and methodologies used.**

   In response to a similar Bill (39-11) DPS examined several areas that have major rental housing projects in the pipeline and that are assumed to be moving forward. This analysis assumes anticipated development in three planning areas (Great Seneca Science Corridor (GSSC); White Flint; and Shady Grove-County Service Park West (CSWP)) and projects the lost impact tax revenue if *all potential* projects took advantage of the proposed bill.

Potential Lost Impact Tax Revenues under Maximum-Loss Scenario

Master/Sector Plan Area	Total Rental Units Supplied	Additional MPDUs	Loss in Transportation Impact Taxes	Loss in School Impact Taxes	Loss in Total Impact Taxes	Cost per Additional MPDU
GSSC	1,550	193	$9,513,900	$8,112,700	$17,626,600	$91,330
White Flint	3,266	408	N/A	$17,094,244	$17,094,244	$41,898
CSPW	1,114	33	$6,837,732	$5,830,676	$12,668,408	$383,891
Total	**5,930**	**634**	**$16,351,632**	**$32,044,676**	**$48,576,308**	**$76,619**

Under the above scenario, the additional 634 affordable units provided under the waiver would result in $48,576,308 in lost impact tax revenue at an average cost to the taxpayer of $76,619 per each additional MPDU constructed.

3. **Revenue and expenditure estimates covering at least the next 6 fiscal years.**

   No additional expenditures are expected as a result of this Bill. Illustrative revenue impacts are described above.

4. **An actuarial analysis through the entire amortization period for each bill that would affect retiree pension or group insurance costs.**

   Not applicable.

5. **Later actions that may affect future revenue and expenditures if the bill authorizes future spending.**

   Not applicable

6. **An estimate of the staff time needed to implement the bill.**

   No additional staff time is needed from DHCA, DPS, and Finance to implement the Bill.

7. **An explanation of how the addition of new staff responsibilities would affect other duties.**

   Not applicable.

8. **An estimate of costs when an additional appropriation is needed.**

   Not applicable.

9. **A description of any variable that could affect revenue and cost estimates.**

   Revenues (or lost impact tax revenues) may be affected by changes in the impact tax rate. The quantity of additional MPDUs developers elect to build may also affect revenues (or lost impact tax revenues).

10. **Ranges of revenue or expenditures that are uncertain or difficult to project.**

    The change in impact tax receipts is difficult to project. Impact tax revenues would vary, depending on the number of developers that elect to build under this waiver.

    Additionally, the market dictates whether projects will be condominium or rentals and it is difficult to predict what future shifts will be. If expected development in different plan areas changes from rental to fee simple sales, fewer projects would make use of the provisions of this Bill. Projects in areas that are now, or were formerly, an enterprise zone are not subject to development impact taxes. Therefore, there would not be lost revenues in these areas. Conversely, the beneficial intent of the Bill would not be realized in these areas either.

11. **If a bill is likely to have no fiscal impact, why that is the case.**

The fiscal impact of this Bill is difficult to determine since it depends completely on the number of developers who avail themselves of this credit.

12. Other fiscal impacts or comments.

Not applicable.

13. The following contributed to and concurred with this analysis: (Enter name and department).

Diane Schwartz Jones, Department of Permitting Services

Hadi Mansouri, Department of Permitting Services

Timothy Goetzinger, Department of Housing and Community Affairs

Dennis Hetman, Office of Management and Budget

Jennifer A. Hughes

Jennifer A. Hughes, Director
Office of Management and Budget

3/31/15
Date

Economic Impact Statement
Bill 8-15, Taxation – Development Impact Tax – Exemptions

Background:

This legislation would exempt the market-rate rental dwelling units in any development which consists of at least 25 percent affordable housing units from the transportation and school development impact taxes.

1. **The sources of information, assumptions, and methodologies used.**

   Sources of information include:
   - Department of Permitting Services (current school and transportation development impact tax rates),
   - Department of Housing and Community Affairs (sample of properties with 250 units including market rates, number of moderately priced dwelling units (MPDUs), and rental rates for MPDUs),
   - McGraw-Hill Construction, Dodge Local Construction Potentials Bulletin (construction costs in Montgomery County for multi-family housing),
   - National Apartment Association ("2013 Survey of Operating Income & Expenses in Rental Apartment Communities"), and
   - Department of Planning.

2. **A description of any variable that could affect the economic impact estimates.**

   The variables that could affect the economic impact estimates are:
   - Current market rental rates,
   - Current rental rates for MPDUs,
   - Current number of MPDUs in the sample of properties provided by DHCA
   - Construction costs,
   - Gross operating profit margin for rental units provided by the National Apartment Association, and
   - The number of unbuilt multi-family dwelling units.

3. **The Bill's positive or negative effect, if any on employment, spending, saving, investment, incomes, and property values in the County.**

   Bill 8-15 could have an impact on the profitability of a new rental development. The impact is based on the assumptions presented in the previous paragraph. Those assumptions include changes to:
   - current market rental rates,
   - current MPDU rental rates,
   - the difference between current market rental rates and current MPDU rental rates,
   - construction costs,
   - school and transportation development impact tax rates, and

- gross profit margin.

Incorporating data provided by DHCA on three sample properties and the National Apartment Association on gross profit margin, Finance estimated the economic effect on business income for new rental property resulting from raising the percent from 12.5 percent to 25 percent.

Under the current policy of providing 12.5 percent rental units at MPDU rates, the benefit to the developer/owner of not incurring both school and transportation development impact taxes in return for charging lower rental rates for MPDU units varies by property. For example, given the three sample properties provided by DHCA, the benefit would expire between six and ten years. That is, for the developer/owner the number of years that the developer/owner would benefit from the exemption of paying the school and transportation development impact taxes versus the loss of revenues from MPDU rental units is a benefit between six and ten years. After that period, the amount of annual rental income earned by the developer/owner over the remaining life to the property is less than the annual rental income if all units paid the market rental rate.

For one of the sample properties, there are 43 MPDUs out of a total of 347 units or 12.6 percent of the total units pay MPDU rental rates. Based on the difference between the current market rental rate and the MPDU rental rate, the development loses approximately $963,000 per year due to the difference in the rental rates. With the exempted amount of $6.3 million in school and transportation development impact taxes, the exempted amount will cover nearly seven years in lost rental revenues. The coverage in the loss of revenues depends on the difference between the development's market rental rate and the MPDU rental rate and the number of units qualifying as MPDUs.

Under the proposed policy of providing 25.0 percent rental units at MDPU rates, that coverage of lost rental revenue and the exemption from the school and impact development impact taxes is between three and five years based on the sample properties and on the current rental rate differential and the number of MPDU units. Using the same example as in the previous paragraph, the number of MPDUs would increase from the current 43 units to 86 units and would result in an annual loss of approximately $1.9 million in rental revenues. With the same exempted amount of $6.3 million, the exemption would cover only three years of the lost revenue.

Therefore, over the short period of two to three years, Bill 8-15 would have a positive economic benefit to rental property developers and owners. However, that benefit would end after that period because the amount of lost rental income would be greater than the amount saved from the exemption of development impact taxes.

The impact of Bill 8-15 is based on the sample of properties provided by DHCA and the inability and lack thereof of increasing market rental rates compared to MDPU rental rates such that the difference remains constant over the life of the property. If the developers/owners of the rental property had the ability, or market power, to raise market rental rates such that the difference between market rates and MPDU rates increased, then the developers/owners would not incur a loss of rental income (assuming operating expenses remaining constant) and the developers/owners would maintain their current operating profit margin of fifty-five percent.

Finally, data provided on the Department of Planning's website state that the number of unbuilt multi-family units in the pipeline is 27,899. Under the current policy of 12.5 percent set aside, the number of MPDUs is approximately 3,490 units. Increasing that percentage to 25 percent would increase the number of units by 3,490 for a total of 6,980. Therefore, Bill 8-15 would increase the number of MPDUs by providing low-income families an increase in the number of affordable rental housing and thereby providing an economic benefit to low-income families.

4. **If a Bill is likely to have no economic impact, why is that the case?**

   Bill 8-15 would have an economic benefit to the developer/owner over a short period of time. But that benefit period is reduced compared to the current policy of 12.5 percent and assumes that the developer/owners do not have the ability to raise market rental rates above the current difference between those rates and rental rates for MPDUs. To offset the estimated deleterious financial effect on the developers'/ owners' revenues, there is an economic benefit to low-income families due to an increase in the number of affordable rental units. However, without precise data on the revenue loss to developers/owners and the economic benefit to low-income families, it is difficult to determine with any accuracy the total economic impact, either positive or negative, on the County.

5. **The following contributed to or concurred with this analysis**: David Platt, Mary Casciotti, and Rob Hagedoorn, Finance.

Joseph F. Beach, Director
Department of Finance

3/20/15
Date

Agenda Item 5
May 7, 2013
Action

MEMORANDUM

TO: County Council

FROM: Michael Faden, Senior Legislative Attorney
Glenn Orlin, Deputy Council Staff Director
Linda McMillan, Senior Legislative Analyst

SUBJECT: **Action:** Bill 39-11, Taxation – Development Impact Tax - Exemptions

Government Operations and Fiscal Policy Committee recommendation: enact with amendments.

Bill 39-11, Taxation – Development Impact Tax - Exemptions, sponsored by Councilmembers Floreen and Rice, then-Council Vice President Navarro, and Councilmember Ervin, was introduced on December 6, 2011. Bill 39-11 would exempt the market-rate rental dwelling units in any development which consists of at least 25% affordable housing units from the transportation and school development impact taxes.

A public hearing was held on January 24, 2012 (see testimony, ©17-24). Representatives of the Housing Opportunities Commission, Maryland-National Capital Building Industry Association, and Montgomery Housing Partnership all urged that the Bill be broadened to cover sale as well as rental units. Attorney Jody Kline also urged that the Bill exempt productivity housing units in non-residential zones. Jim Humphrey of the County Civic Federation opposed the Bill, suggesting that the Council revisit it when the County's fiscal situation improves. Also see the letter from the Walter Johnson cluster PTA on ©25-26, opposing the diversion of school impact tax funds.

Government Operations and Fiscal Policy Committee worksessions were held on February 25 and April 4, 2013. At the first worksession, Committee members directed Council staff to develop estimates of foregone impact tax revenue, assuming that the bill would not apply to already approved subdivisions or to any development on public land, and assuming various limits on the exemption available in a given year and various sunset provisions.

Fiscal impact estimates

OMB An OMB/Finance Department fiscal and economic impact statement (see ©5-14) concluded that the exemption allowed under this Bill could result in an impact tax revenue loss of as much as $56.7 million. Council staff believed that this estimate may be substantially overstated because, among other reasons:

- it assumed that no transportation impact tax credits would be granted on account of the housing built in specific areas with major transportation programs; and
- it appears not to take into account a provision in current law (County Code §52-90(d)) which reduces the school impact tax by 50% for any non-exempt dwelling unit located in a development where at least 30% of the dwelling units are MPDU's or other affordable units.

The OMB fiscal impact statement calculated that the impact tax revenue loss per added affordable housing unit in selected areas would range from $38,525 to $446,227, and would average $89,449. The breadth of these estimates suggests the difficulty of generating them. This also assumes, as OMB noted, that this exemption will give developers sufficient incentive to actually use it, about which Finance Department staff in the economic impact statement was skeptical (see ©11-14).

Council staff Using a simple method, Council staff initially estimated the impact tax revenue loss from a hypothetical 100-unit 2-bedroom garden apartment development, not located in an enterprise zone, in which the developer would increase the number of MPDU's from 15% to 25% to take advantage of the exemption in this Bill. We calculated the impact tax lost per each of the 10 added MPDU's, at current impact tax rates, to be $163,744.[1]

At the February 25 worksession the Committee asked for Council staff's best estimate of the fiscal impact of Bill 39-11 if the Bill were amended to exclude both already-approved subdivisions and developments on public land (where the value of the land was reduced as part of a development agreement that requires a certain number of affordable units.) from its impact tax exemption. Council staff conferred with staffs from M-NCPPC (Richard DuBose and Roberto Ruiz), the Departments of Permitting Services (Reggie Jetter) and Finance (David Platt and Mike Coveyou), and the Office of Management and Budget (Mary Beck) in developing our assumptions and analysis.

One assumption we made is that the only developments that would take advantage of the exemption would be multi-family residential or multi-family mixed-use projects. The Bill as introduced exempts only rental units from the impact tax, and it is unlikely that a development of rental attached or detached single family homes would use this provision.

Another assumption we used is that no additional affordable housing units resulting from Bill 39-11 would occur in the next 3 years. Data from M-NCPPC and DPS indicate that 3 years is the average time between site plan approval for multi-family residential buildings and the time their impact tax payments would be due. If this Bill is enacted this spring, it likely would have no effect — and so, would not reduce impact tax revenue -- in FYs 14-16. The revenue loss would begin in FY17, the second-to-last year of the current CIP.

[1]The calculation was: impact taxes per unit (school $11,358 + transportation $7906 = total impact tax/unit $19264) x 85 tax-forgiven units = $1,637,440 total impact tax revenue loss/10 added MPDU's = $163,744 revenue loss per added MPDU.

M-NCPPC's Center for Research and Information Systems estimated that, under current master plans, about 55,000 multi-family units yet to be built are not already in the pipeline of approved subdivisions. During 2001-2010 only 5.3% of the units were built in what are now State-designated Enterprise Zones (EZ's), where impact taxes are not collected: Wheaton CBD, Long Branch, and Gaithersburg Town Center. However, this percentage does not include Silver Spring CBD, which is no longer an EZ but is treated as one for impact tax purposes. The State is considering establishing an EZ in Glenmont, and the County has already exempted the White Flint special taxing district from payment of the transportation impact tax.

Taking these factors into account, Council staff believes that about 15% of all multi-family units would not be subject to impact taxes, reducing the number of units in developments where impact taxes would be levied to 46,750. Assuming that each of these developments must meet the minimum 12.5% MPDU requirement — and knowing that the MPDU's themselves are already exempt from impact taxes, as the law provides —the impact tax would apply to about 40,900 units. Finally, the number of units in known multi-family dwellings to be built on County land — County Service Park West (Shady Grove) and the Public Service Training Academy (Great Seneca Science Corridor) — is about 2,700, bringing the number of units where the tax would be apply down to about 38,200.

The loss of impact tax revenue also depends on the split between garden apartments and high-rise units, since the rates differ between them. The rates that will apply on July 1, when the 8.7% inflation index takes effect, are:

	Garden apartments	High-rise apartments
School Impact Tax	$12,346/unit	$5,234/unit
Transportation Impact Tax		
Metro Station Policy Areas	$4,297/unit	$3,090/unit
General District	$8,594/unit	$6,181/unit

During 2001-2010, about 20% of multi-family units were garden apartments with two or more bedrooms, and 80% were high-rise units (which, for impact tax purposes, also include studio and one-bedroom garden apartments). We assumed that only 25% of the 38,200 units would be located in the remaining, non-exempt Metro Station Policy Areas: Friendship Heights, Bethesda CBD, Grosvenor, Twinbrook, Rockville Town Center, and Shady Grove; and that the rest would be built elsewhere. Therefore, if all future multi-family developments were to take the exemption offered by this Bill, amounting to about 5,500 more affordable units over the rest of the County's buildout, the exemption would result in an aggregate impact tax revenue loss of $477 million, or about $87,000 of revenue for each added affordable unit. (Calculated in a very different way, OMB's Fiscal Impact Statement estimated a revenue loss of about $89,000 for each added affordable unit.) Our calculations are shown below:

New affordable units: 38,200 total units x 0.125/0.875 = 5,457 ~ 5,500 affordable units

School tax lost: 38,200 total units x 0.20 garden units x $12,346/unit = $94.3 million
38,200 total units x 0.80 high rise x $5,234/unit = $160.0 million
Total = $254.3 million

Transportation tax lost:

38,200 total units x 0.25 Metro x 0.20 gardens x $4,297/unit = $8.2 million
38,200 total units x 0.75 General x 0.20 gardens x $8,594/unit = $49.2 million
38,200 total units x 0.25 Metro x 0.80 high rise x $3,090/unit = $23.6 million
38,200 total units x 0.75 General x 0.80 high rise x $6,181/unit = $141.7 million
Total = $222.7 million

Of course, for other reasons not every developer will increase its share of affordable units in return for an exemption on its impact taxes. So the challenging part of any fiscal impact estimate is to hypothesize how many developers in a given time period would be likely to take this option. In our educated guess, not more than one building a year is likely to do so, and its developer is likely to be a mission-driven organization rather than a conventional developer.

Thus an alternative way to estimate this Bill's fiscal impact is to make an assumption about how many developments that use this option might be completed in any fiscal year and what a likely building might consist of. For example, if a 175-unit multi-family building has 6 efficiency units, 115 one-bedroom apartments, 50 two-bedroom apartments, and 4 three-bedroom apartments (this distribution is modeled after a building in Wheaton), the minimum requirement for MPDU's is 22 units (12.5%). The impact tax revenue loss would be $1.8 million if the building were located in a Metro Station Policy area, or $2.45 million if it were in the General District. The cost for each added MPDU (22) in the Metro Station Policy Area would be about $81,600, and in the General District about $111,520. Assuming that the impact tax for one such building would be due in FY17, **we would reduce the impact tax revenue estimates by about $2.1 million in FY17 and in FY18 (and every year thereafter), split between the transportation ($1 million/year) and school ($1.1 million/year) taxes.**

Issues and options/Committee recommendations

At the Committee worksessions held on February 25 and April 4, the Committee discussed the following issues and recommended several amendments to the Bill, which are incorporated in the Committee redraft on ©1-3A:

Balance In Council staff's view, the central issue this Bill raises is how best to allocate scarce County funds to promote affordable housing. The Draft 2012 County Housing Policy, now before the Planning, Housing, and Economic Development Committee, includes action plans and recommendations for increased incentives such as this Bill would provide. The Policy recommends that the County should "explore financial and other incentives for high-rise rental development to make the construction of MPDU's more feasible, especially for projects providing more than the minimum number of MPDU's and for those providing units with more bedrooms", that the County should "create and design incentives that will lead to the construction of well-located affordable rental housing", and that the County should "consider incentives such as increased heights, additional density, waiver of transportation and school construction impact taxes and fees from the Washington Suburban Sanitary Commission

(WSSC), and other fees and taxes that contribute to increased cost of developing affordable housing."

The critical question then is whether an estimated $2.1 million each year is best spent to increase the number of MPDU's in any single applicable rental building, or to send the same amount of funds to the Housing Initiative Fund (HIF), where they could be targeted as a grant or repayable loan for a specific project. The same funds could also be allocated to increase the ceiling on non-HOC Payments in Lieu of Taxes (PILOT's). Many projects where the HIF is used to provide interim or low cost financing in exchange for additional MPDU's result in additional affordable housing at no or low cost to the County. Conversely, creating permanent affordable housing that does not depend on an ongoing subsidy for very-low-income people can be costly on a per-unit basis. Very-low-income people are not generally able to be housed in an MPDU without an ongoing subsidy, and those units are unlikely to be built without a County contribution.

Cost-saving modifications The Committee considered ways to more narrowly channel this kind of exemption in order to make it a more efficient use of County funds. No Committee member expressed interest in broadening the Bill's scope to include sale units, as several speakers at the hearing proposed.

Applicability Should this exemption, if enacted, only apply to developments that have not already received preliminary subdivision approval or site plan approval? The Committee agreed with Council staff that developments which have gone beyond those points arguably have already "made their pro forma's" and don't need further County assistance.

Committee recommendation: exclude developments that received subdivision or site plan approval before this Bill takes effect.

Publicly owned land Should developments on publicly owned land be eligible for an exemption? (Publicly-owned land, rather than only County-owned land, would include, for example, school or WMATA property.) The Committee concluded that the tax exemption should not apply to any development on publicly owned land where a lower value of the land was part of a negotiated development agreement that required more than the minimum number of affordable housing units.

Committee recommendation: exclude developments on publicly-owned land.

Zoning credits Similarly, should developments which receive extra density for furnishing more affordable housing units be eligible for this kind of exemption? Committee members considered whether to exclude from this exemption developments that receive a zoning benefit, such as extra credits under a CR zone, for providing more affordable housing.

Committee recommendation: exclude developments that have received a zoning benefit for providing more units of affordable housing.

Higher thresholds Is 25% the optimal amount to trigger an impact tax exemption? HOC and others who were consulted when this Bill was drafted concluded that 25% was the highest the exemption could go and still let the numbers work to move forward with a development. HOC staff noted that the 25% ceiling came from "mission driven" developers. On the other hand, in Bill 11-12 last year the Council selected 30% as the level of affordable housing that would be substantial enough to shorten the property disposition process, and DHCA generally seeks at least 30% affordable housing in projects developed on publicly owned land.[2]

Committee recommendation: leave the affordable housing threshold at 25%.

Dollar or unit limits Should the law limit the number of units eligible for this exemption each year, or the amount of County funds allocated, much like the current system to set the level of payments in lieu of taxes (PILOT's)? Committee members discussed setting either an annual unit limit or revenue loss limit, or both, but did not decide on any specific limits.

Committee recommendation: do not set any specific dollar or unit limits on this exemption.

Sunset If this exemption approach (or any variant of it) is used, should it be sunset after several years to see whether it has in fact accomplished its goals at a reasonable cost?

Committee recommendation (2-1, Councilmember Ervin dissenting): do not sunset this exemption, but review it periodically.

This packet contains:	Circle #
Bill 39-11 with Committee amendments	1
Legislative Request Report	4
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Current County impact tax rates	15
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[2]Since the Bill's language refers to "a *development* in which at least 25% of the dwelling units are exempt" (see ©2, lines 19-20, and ©3, lines 50-51) (emphasis added), if more than 25% of the units in a single building in that development are affordable units, that fact would not make the market-rate units in that building or those in the entire development exempt from the impact tax under this Bill.

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March 3, 2015

The Honorable George Leventhal
President
Montgomery County Council
100 Maryland Avenue
Rockville, MD 20850

Dear Council President Leventhal:

On behalf of Montgomery Housing Partnership (MHP), please allow me to take the opportunity to share some thoughts on Bill 8-15 Taxation - Development Impact Tax - Exemption. MHP fully supports the Council's continued focus on the critical need to address the affordable housing crisis in Montgomery County.

Many of you are familiar with MHP's role within the County as a developer of affordable rental multi-family communities, but just to give a couple of updates: Five months ago we broke ground on The Bonifant in downtown Silver Spring. We are on schedule and budget to bring almost 150 affordable rental units for seniors to the downtown area. Additionally, 93 of the 114 homes at Olney Springs have been bought and occupied, with another 11 sold.

The most recent projections show a need for an additional 60,000 – 100,000 housing units by 2030 to meet demand, with a majority of these units serving low-to-moderate income households. Currently, Montgomery County is issuing building permits for only about 3,000 units annually – a rate we'd need to double to meet the projected demand. The County needs to think outside of the box on how we can fill this gap. Bill 8-15 does that, by providing incentives to developers to voluntarily produce more moderate income units.

Exempting rental projects that provide a minimum of 25 percent Moderately Priced Dwelling Units overcomes one of the major obstacles to affordable construction in the County. As it currently stands, each dwelling unit has an approximate $30,000 price tag from Impact Taxes alone. Adopting Bill 8-15 increases the supply of MPDUs and concurrently reduces the costs, and subsequently the price, of market rate rental units.

We strongly support a program that will eliminate or reduce the Impact Tax burden on new housing through the provision of additional affordable units, helping the County to meet its repeatedly stated goal of addressing the affordable housing shortage, and increasing the supply of housing for low and moderate income households. Additionally, we encourage the Council to consider the feasibility of expanding this exemption to for-sale projects also.

Thank you for taking the time to consider these thoughts and for always keeping the needs of Montgomery County citizens at the forefront of your mind. We look forward to the opportunities to continue to work with the County ensuring all our residents live in quality, safe, affordable communities.

I welcome the opportunity to discuss this issue with you further. Please feel free to reach me at rgoldman@mhpartners.org or 301-812-4114.

Sincerely,

Robert A. Goldman, ESQ.
President