FROM

NAME & TITLE	Edward J. Gallagher, Director
AGENCY NAME & ADDRESS	Department of Finance Room 454, City Hall (396-4940)
SUBJECT	City Council Bill No. 08-0010R

CITY of BALTIMORE

MEMO

CITY OF BALTIMORE 1797

TO

The Honorable President & Members
of the City Council
Room 400, City Hall

DATE:

February 15, 2008

Attn: Ms. Karen Randle

City Council Bill 08-0010R invites the Co-Chairs and Members of the Mayor's Blue Ribbon Committee on Taxes and Fees to share with the City Council the Committee's findings on alternate revenue options and other viable measures that can be implemented to reduce Baltimore City's property tax rate over the next several years. The Department of Finance served as staff to the Committee, which consisted of 29 members and two co-chairs.

Committee members should be recognized for their contribution of significant time and effort. The Committee held 15 meetings, beginning in March and continuing through December, in its effort to learn why the City's property tax rate is as high as it is relative to other Maryland counties and to develop a menu of options that would allow a property tax rate reduction by replacing the lost revenues with new or enhanced revenue sources. More than 16 different options were considered.

Included with this bill response is a copy of the Executive Summary of the report of the Blue Ribbon Committee. Members of the Committee, including Co-Chair Jody Landers, look forward to discussing the Committee's findings and recommendations in more detail with the City Council at the upcoming hearing.

comments

City of Baltimore

Report of the
Blue Ribbon Committee on Taxes and Fees

Final Draft

City of Baltimore

The Honorable Sheila Dixon, Mayor

Blue Ribbon Committee

Joseph T. Landers, III, Co-Chair
The Honorable Joan Pratt, Co-Chair

Public Financial Management

Two Logan Square, Suite 1600
18th & Arch Streets
Philadelphia, PA 19103-2770
215 567 6100
www.pfm.com

Final Draft
December 5, 2007

Mayor's Blue Ribbon Committee on Taxes and Fees

Directory of Members

Co-Chairs:

- The Honorable Joan Pratt, *Comptroller City of Baltimore*
- Joseph T. Landers III, *Executive Vice President Greater Baltimore Board of Realtors*

Committee Members:

- Timothy D. Armbruster, *President and CEO, Goldseker Foundation*
- Diane Bell-McKoy, *President & CEO, Associated Black Charities*
- Kirsten Sandberg Caffrey, *Citizen Representative*
- Dr. Rev. William Calhoun, *Interdenominational Ministerial Alliance*
- Brenda Clayburn, *President, City Union of Baltimore*
- Atwood Collins III, *Executive Vice President, M&T Bank*
- Robert Embry, *President, The Abell Foundation*
- Sean Flanagan, *Citizen Representative*
- Mel Freeman, *President of the Board of Governors, Citizens Planning and Housing Association*
- Donald C. Fry, *President and CEO, Greater Baltimore Committee*
- Tracy Gosson, *Citizen Representative*
- Nina Harper, *Executive Director, Oliver Community and Economic Development Corp.*
- Joel Hendricks, *Deputy Chief of Staff, Maryland Comptroller's Office*
- The Honorable Helen Holton, *Councilwoman, 8th District Baltimore City Council*
- The Honorable Verna Jones, *Senator, 44th District Maryland General Assembly*
- Mark Joseph, *Chairman, of the Board Municipal Mortgage and Equity, LLC*
- Jon M. Laria, *President of the Board Live Baltimore*
- Mystique Lassiter, *Citizen Representative*
- Derrick Lennon, *Glen Neighborhood Improvement Association*
- Josef Nathanson, *Citizen Representative*
- George Nilson, *City Solicitor, City of Baltimore*
- Anthony Rodgers, *Vice President, A&R Development*
- David Rudow, *Founder, Board Member, and President Baltimore Efficiency and Economy Foundation, Inc.*
- Joe Louis Ruffin, *Gotham Development*
- Mayo A. Shattuck, *President, Chairman, and CEO Constellation Energy*
- C. William Struever, *Co-Founder, Partner, CEO & President Struever Bros. Eccles & Rouse, Inc.*
- Hector Torres, *President, Prosaber Consulting*
- Otis Warren, *President and CEO, The Otis Warren Group*
- Michael Yerman, *Broker, Yerman, Witman, Gaines & Garceau Realty*

EXECUTIVE SUMMARY

Executive Summary

The property tax rate in the City of Baltimore is approximately twice as high as the average rate in surrounding counties. A homeowner in Baltimore City whose home is assessed at $150,000 pays up to $3,402 annually in real property taxes, while in Baltimore County a home assessed at the same value is taxed at $1,650. The disparity is even more pronounced for large commercial properties. Taxes on a $25 million property in the City total $567,000. In Baltimore County, the same property has an annual tax bill of just $275,000. It is easy to see why potential homeowners and commercial property owners might hesitate before purchasing property in the City.

Despite this competitive disadvantage, the City has enjoyed some success in attracting both residents and businesses. In a reversal of fortune, Baltimore's population is estimated to have actually increased in 2006 - the second such increase since 1971. While census estimates put that increase at just 897 residents, it represents a major departure from the 1990's when the City lost an average of approximately 8,500 residents per year. Current development projects underway in 2007 are valued at approximately $3.0 billion, including the first residential building at the East Baltimore Development Initiative and seven major biomedical and life science projects. In addition, expansions in major health and hospital institutions are expected to generate more than 12,000 jobs over the next five years. Finally, current projections estimate that 2,552 new households and 3,145 new jobs will relocate to the City between now and 2018 due to Base Realignment and Closure (BRAC). These trends indicate Baltimore's potential for growth and demonstrate the critical timing of this report.

Still, Baltimore's property tax rate - $2.268 per $100 of assessed value in FY2008 – is a major barrier to the City's growth and development. Lowering the rate could unlock the City's unrealized potential and trigger a significant increase in the real property base. In turn, this would increase property tax revenue and allow for further investment in the City's future in the form of an even lower tax rate, enhanced services, or a combination of both.

On February 15, 2007, Mayor Dixon appointed a 26 member[1] Blue Ribbon Committee to study the City's tax and fee structure and recommend ways to make a significant reduction in the property tax rate. The Committee, representing the City's residents, businesses, non-profit institutions, City Council, City Comptroller, City administration, and State officials, was charged with establishing recommendations for reforming the local tax and fee structure for the purpose of reducing the property tax rate and supporting the City's long-term fiscal health.

The Committee firmly believes that a rate reduction in itself would eventually result in growth in property tax revenue and therefore allow a reduced property tax rate. Its members also realize that the City cannot commit to a substantial rate reduction without replacing the resulting revenue loss. Therefore, the Committee looked to develop a menu of options that would allow a property tax rate reduction by replacing the lost revenue with new or enhanced revenue sources.

This report presents two options developed by the Committee to show alternative scenarios for property tax reduction. The first is intended to have maximum short-term impact, and is

[1] A full list of the Blue Ribbon Committee's members and their affiliation can be found in Appendix 5 of this report.

comprised of options which can be implemented over the next year to reduce the property tax rate to about $2.00 from $2.268. The second scenario includes options that will take longer to implement, but will lead to deeper reductions close to the Committee's target level.

It should be noted that just as the Committee was wrapping up its final recommendations, the Governor convened a Special Legislative Session of the Maryland General Assembly to address the State's structural deficit, estimated at $1.65 billion for FY 2009. While the full impact of Session's outcomes are still under analysis and not yet fully known, several measures which passed have a direct bearing on the recommendations contained in this report. Some of the most significant measures include:

- An increase in the State sales tax rate from 5 percent to 6 percent;
- A requirement that controlling interests in the transfer of ownership of commercial properties pay State property transfer tax as well as local property transfer and recordation taxes on the value of the transfer;
- A constitutional amendment authorizing up to 15,000 video lottery terminals at five locations in Maryland (including a location in Baltimore City), subject to approval by the voters in the November 2008 general election.

In addition, several measures were passed that will negatively impact revenue and State aid to the City, particularly in the areas of income tax revenues, transportation, Program Open Space and education funding. It is useful to bear these very recent developments in mind when considering the Committee's recommendations that follow. There will likely be additional State legislative and budget changes that add more financial burden to the City when the 2008 General Assembly Session gets underway in January.

Short Term Scenario

After careful consideration of the sixteen options detailed in the body of this report, the Committee developed a scenario in which actions implemented over the next year or two could reduce the property tax rate by $0.248 per $100 of assessed value. While the City's commendable efforts to reduce the rate by two cents per $100 of assessed value each year beginning in 2005 represent a firm commitment to an annual goal for property tax relief, the time is right for a more dramatic reduction.

With two exceptions, the options presented in the following scenario are steps the City can take on its own without approval from the State. If state action is requested to allow further and more significant rate reductions, it is important for the City to demonstrate maximum effort before asking for additional assistance. The exceptions are the two options dealing with transfers of controlling interests of business entities, both of which require changes to State law. Of all options reviewed by the Committee that require state action, these are believed to already have the strongest support in the Maryland General Assembly. In addition, the State's projected budget deficit of approximately $1.7 billion provides an incentive for implementation of both options, as they would generate significant state revenue.

While not every Committee member supported each separate option individually, the Committee agreed that a package of multiple options affecting different stakeholders was needed to achieve meaningful and fair property tax reduction. Each option has potential benefits and drawbacks that are outlined in the body of this report. However, by clustering a set of options together, the Committee has demonstrated that a significant property tax cut *is* possible if there is a firm commitment from the City, its legislative representatives, and its citizens and businesses.

The following table presents a scenario that would cut the real property tax rate by $0.248 per $100 of assessed value in two years – a ten percent decrease from FY2008 and more than eleven times the committed FY2008 reduction of two cents per $100:

Short Term Scenario
$0.251 Reduction in One to Two Years

Option	Revenue Potential ($ millions)	Rate Reduction (per $100)	Location in Report
Increase the Homestead Credit Cap to 10%	$24.2	$0.092	p. 43
Raise the Income Tax Rate to 3.20%	$12.1	$0.045	p. 49
Continue 2-Cent Reduction through FY2010 (two additional years)	$0.0	$0.040	p. 5
Transfer Tax on Transfers of Controlling Interests	$4.7	$0.020	p. 80
Require All Controlling Interest Transfers to be Reported to SDAT	$4.0	$0.015	p. 82
Further Coordination Between the City and SDAT, Other Improvements to the Assessment Process	$4.0	$0.015	p. 84
Increase the Hotel Tax Rate to 10%	$4.1	$0.013	p. 52
Comprehensive Fee Analysis	$1.0	$0.004	p. 55
Aggressive Vacant Property Fee	$0.8	$0.004	p. 88
Total	**$54.90**	**$0.248**	
	Current Real Property Tax Rate	**$2.268**	
	New Real Property Tax Rate	**$2.020**	

Options Included in the Short Term Scenario

Increase the Homestead Credit Assessment Cap to 10 Percent
The Homestead Credit is a cap on the growth in taxable assessed property value. The assessment cap only applies to owner-occupied residential property and is designed to protect homeowners from large increases in property tax obligations due to reassessment. The State of Maryland requires that the local property tax cap be set between zero and ten percent; Baltimore's is set at four percent. If the City were to increase the assessment cap to the State limit, it would realize an additional $24.2 million in revenue in FY2009. However, the City is required to notify the State of any change to the cap by November 15 of the preceding fiscal year. Because City Council must vote on such a change before the State is notified, it is unlikely that this option can be implemented until FY2010.

Increase the Income Tax Rate to 3.20 Percent

Increasing the City's current 3.05 percent income tax rate to the maximum 3.20 percent allowed by state law would generate approximately $12.1 million in new revenue in FY2009 and would allow the property tax rate to be lowered by $0.045 per $100 of assessed value. To make a change in the income tax rate the City must notify the State by July 1 of the preceding calendar year. Therefore, the earliest this option could be implemented is January 1, 2009.

Continue Two-Cent Reduction

In FY2005, the City established a goal of reducing the real property tax rate by $0.02 per $100 in assessed value each year for five years. Mayor Dixon has made that reduction for FY2008 and could do so again in FY2009 and FY2010. This would reduce the property tax rate by $0.020 per $100 of assessed value each year for a total of $0.040.

Require Transfer and Recordation Taxes to be Paid on Transfers of Controlling Interest

When property is transferred as part of a controlling interest transfer, recordation and transfer taxes are not required to be paid. This option would eliminate that exception and generate approximately $4.7 million and allow a property tax rate reduction of $0.020 per $100 of assessed value.

Require All Controlling Interest Transfers to be Reported to SDAT

When properties are transferred as part of controlling interest transfers, the prices paid for those properties are not publicly recorded or reported to the Maryland State Department of Assessment and Taxation. The sale price is an important piece of the assessment process, and without it SDAT has fewer tools for properly assessing the value of these properties, which are often high in value. Requiring transfers of controlling interests to be reported to SDAT would yield an estimated $4.0 million in City revenue and allow a property tax rate reduction of $0.015 per $100 of assessed value.

Improved Coordination Between the City and SDAT; and Further Improvements to the Assessment Process

SDAT's first priority is the fair, accurate, and consistent assessment of all taxable property in the State. It does not have a vested interest in city and county property tax revenue. Although local governments do not have the power to assess property, they can monitor SDAT assessments and appeal when they believe a property is underassessed. In addition, the City could improve its coordination with SDAT and share data to help to improve the accuracy of the agency's assessments. Improving the assessment process and better coordinating with SDAT could help the City recover approximately $4.0 million in revenue and allow a property tax rate reduction of $0.015 per $100 of assessed value.

Increase the Hotel Tax Rate to 10 Percent

The current hotel tax rate is 7 percent. Raising the rate to 10 percent would generate $4.1 million in new revenue. This option would yield an estimated $4.1 million in City revenue and allow a property tax rate reduction of $0.013 per $100 of assessed value.

Comprehensive Fee Analysis
A comprehensive review of all fees, fines, and charges for service would ensure that the City charges enough to cover its costs for those services. Changes made to the fee structure as a result could generate approximately $1.0 million in additional revenue, allowing property tax reduction of $0.004 per $100 of assessed value.

Aggressive Vacant Property Fee
The City should investigate charging a more aggressive fee for vacant property registration. The current fee charged is $30 per year, but other cities have charged as much as $5,000 for registration of property that has been vacant for ten years. Given current estimates of 17,000 vacant properties in the City, potentially significant revenue could be generated from higher registration fees. For this report, potential revenue generated by this option was conservatively estimated at $850,000, allowing a modest rate reduction of $0.004. However, the real benefit of any strategy that creates an incentive to rehabilitate and occupy vacant or abandoned properties is the eventual increase in the City's property tax base.

Other Major Revenue Options
In addition to the options outlined above, the Committee also examined other long-term alternatives that the City can pursue to provide substantial additional property tax reduction when adopted in combination with the short term options. The following list contains five such options that require State action and might take some time to implement, but would allow significant rate reduction. There was not a clear consensus among Committee members in favor of these options, in part because they were seen as difficult to implement. However, they do represent potentially large sources of revenue needed to help the City meet its property tax reduction goal:

Other Major Revenue Options

Option	Revenue Potential ($ millions)	Rate Reduction (per $100)	Location in Report
1% Local Option Sales Tax	$64.4	$0.236	p. 62
1% Regional Sales Tax	$63.1	$0.230	p. 66
1% Tax on Commuter Wages	$75.7	$0.240	p. 74
1% Local Earnings Tax	$47.4	$0.162	p. 69
Gaming Revenue	$45.9	$0.170	p. 76
Total	**296.5**	**$1.038**	

Note: It is likely that only one of the sales tax options and one of the commuter/local earnings taxes could be implemented at one time, and they were considered mutually exclusive by the Committee.

Options Included in Other Major Revenues

Local Option Sales Tax
Establishing a one percent sales tax for all taxable goods sold in the City would generate approximately $64.4 million in FY2009 and allow a property tax reduction of $0.236 per $100 of assessed value. If the State sales tax rate remains at five percent, this option would increase the aggregate sales tax rate in Baltimore to six percent. According to State law, subdivisions cannot levy a general sales tax; therefore, this option would require the passage of state legislation.

Regional Sales Tax
A regional sales tax differs from a local option sales tax in that the additional one percent rate would be levied on several counties in the greater Baltimore region rather than in the City alone. In addition, half of the revenue generated by the tax would be used to pay for cultural assets in the region. The other half would be distributed back to the counties and to the City according to a formula based on tax capacity and effort. This option would generate an estimated $63.1 million for the City in FY2009 and allow a $0.230 reduction to the property tax rate. Like the local option sales tax, a regional sales tax would require State legislation.

Commuter Wage Tax
The City's income tax revenue is derived only from its residents. Individuals who work in the City but do not live in the City are taxed by their county of residence. This option would generate approximately $75.7 million by taxing those commuters on one percent of the wages they earn within city limits. This option, which would permit a property tax reduction of $0.240 per $100 of assessed value, requires state legislation.

Local Earnings Tax
This option differs from the pure commuter tax by taxing the wages of *all* individuals who work in the City. This would be a statewide option, so that each county could opt to levy the additional tax. Further, individuals could deduct the tax from the existing income tax they pay to their county of residence. In most counties, net income tax revenue would be reduced as a result of this option. In the City of Baltimore, approximately $47.4 million in new revenue would be generated, allowing a property tax reduction of $0.162 per $100 of assessed value. Implementing this option would require state legislation.

Gaming Revenue
For several years, various Maryland Governors and the State General Assembly have considered legalizing slots and casino gambling to augment State revenues and support the ailing thoroughbred horse-racing industry. With the State facing a significant budget deficit next year, these revenue raising alternatives are expected to be considered once again. Experts appearing before the Blue Ribbon Committee suggested that the State's need for revenue could potentially lead to the adoption of limited gaming in Maryland. Many Committee members expressed the view that the City should receive a share of revenue if legislation allowing gaming in Baltimore passes. Through a revenue-sharing scenario presented in the body of this report the City could realize an estimated $45.86 million, allowing a property tax rate reduction of approximately $0.170 per $100 of assessed value.

Long Term Scenario
To show the potential impact of these longer-term revenue options, the Committee developed a second scenario that adds two of the foregoing additional options to the Short Term Scenario presented earlier. Both of these – a local option sales tax and additional revenue generated by casino and slots gaming located in the City – require new state legislation. Of the five long-term options considered by the Committee, these two received the strongest support. Because both options could take some time before they are implemented, this set of options can be considered a long-term scenario for property tax relief. If all of the options listed in the Long-Term

Scenario below were to be implemented, Baltimore's property tax rate could be reduced by $0.654 to $1.614 – a 28.8 percent decrease.

Long Term Scenario
$0.653 Reduction Over Several Years

Option	Revenue Potential ($ millions)	Rate Reduction (per $100)	Location in Report
Increase the Homestead Credit Cap to 8%	$24.2	$0.092	p. 43
Raise the Income Tax Rate to 3.20%	$12.1	$0.045	p. 49
Continue 2-Cent Reduction (2 years)	$0.0	$0.040	p. 5
Transfer Tax on Transfers of Controlling Interest	$4.7	$0.020	p. 80
Require All Controlling Interest Transfers to be Reported to SDAT	$4.0	$0.015	p. 82
Further Coordination Between the City and SDAT, Other Improvements to the Assessment Process	$4.0	$0.015	p. 84
Increase the Hotel Tax Rate to 10%	$4.1	$0.013	p. 52
Comprehensive Fee Analysis	$1.0	$0.004	p. 55
Aggressive Vacant Property Fee	$0.8	$0.004	p. 88
Local Option Sales Tax	$64.4	$0.236	p. 62
Gaming Revenue	$45.9	$0.170	p. 76
Total	**$165.20**	**$0.654**	
New Real Property Tax Rate		**$1.614**	

Other Options
In addition to the options presented above, the Committee considered other alternatives. The remaining three options, discussed at length in the body of this report, are:

- Transfer additional functions to the State of Maryland (p. 91).
- Charge a fee for solid waste collection (p. 57).
- Develop a new strategy for tax-exempt property (p. 59).

The first two options, transferring additional functions to the State and charging a solid waste collection fee, were not included in either scenario because they did not receive a great deal of support from the Committee. The third option, developing a new strategy for tax-exempt property, was not included because the estimated revenue impact (and corresponding rate reduction) cannot be quantified. It did however receive substantial support from the Committee, and specific strategies outlined in the body of this report should also be considered as potential options to increase the City's real property base and lower the property tax rate.

In addition, the Committee recommends that the Mayor appoint an independent group, similar to this Blue Ribbon Committee, to investigate the potential for cost cutting, operational changes and program consolidations that will permit the City to reduce expenditures and further assist the effort to reduce the City tax rate.