


FROM	NAME & TITLE	Henry Raymond, Director <i>H Raymond</i>	CITY of BALTIMORE MEMO	
	AGENCY NAME & ADDRESS	Department of Finance Room 454, City Hall (396-4940)		
	SUBJECT	City Council Bill 15-0585 – Tax Credits – Historic Properties		

DATE:

TO

Honorable President and
 Members of the City Council
 C/O Natawna B. Austin
 Room 409, City Hall

January 14, 2016

This CCB 15-0585 Tax Credits – Historic Properties is for the purpose of renewing the City’s Historic Property Tax Credit. Additionally, the proposed legislation contains amendments to the existing statutory language which would alter the definition of “eligible improvements,” change the scope of the historic tax credit program, increase the amount of construction costs that a project can include and not be subject to the limitations provided in the credit, and alter eligibility requirements to provide “historic” tax credits to high performance market-rate rental housing projects that would not otherwise qualify for the credit. The proposed legislation, in its current form, does not modify certain procedures for adopting rules and regulations governing the credit.

Analysis

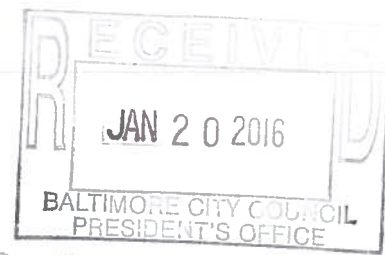
Eligible Improvements and the Scope of the Historic Tax Credit Program

The City’s Commission for Historical and Architectural Preservation (CHAP) has proposed additional language be added to the statute that would alter the definition of “Eligible Improvements” to include requirements already found elsewhere in the statute, and alter the stated goal of the program to include the word “Revitalize.” The Department of Finance will defer to the Planning Department and the CHAP, who are promoting this language.

Increasing the Amount of Construction Costs for Full Credit Projects

When the City originally adopted the Historic Tax Credit authorized by the State, there were limitations placed on the size of projects to which the credit could be applied. Projects with construction costs greater than \$3.5 million were still eligible for an historic tax credit if they met the eligibility requirements, but the credit amount was phased out over time. The authors of the existing statute realized that without such limitations, the amount of tax revenue the City would be forgoing could put the City in a dangerous fiscal situation. As recently as the 2015 legislative session of the General Assembly, the City felt the impact of increasing its tax base without actually recovering the taxes from such an increase.

Fav w/ Amend



When the City experiences increases in its tax base, these increases are factored into calculations used to determine the amount of State aid that the City receives. While increasing the tax base is normally a good thing, even in light of the accompanying reductions in State aid, the City has recently found itself in the worst possible position of increasing its tax base, facing the accompanying reductions in State aid, but also receiving an extremely reduced increase in actual tax revenue. PILOTs, TIFs and tax credits all contribute to this issue. While all of these programs are important to the continued economic growth of the City, the current fiscal situation the City faces requires the prudent management of these programs. Accordingly, now is not the time to expand the losses associated with these programs.

By expanding the size of projects that qualify for a full Historic tax credit to \$5.0 million, the City would essentially be forgoing additional tax revenue while continuing to experience the accompanying negative effects experienced through the State's aid calculations. The current level of \$3.5 million provides ample opportunity for most projects to receive the full credit, while still providing the City a prudent level of protection against large losses of revenue from larger projects exploiting the generosity of the Historic tax credit program. For these reasons, the Department of Finance strongly recommends that the limitation on construction costs eligible for the full credit currently found in the statute be maintained and the increase in the proposed legislation be struck in accord with the attached amendment #1.

Elimination of Existing Eligibility Requirements for High Performance Market Rate Rental Housing Projects

The City has fully adopted a tax credit program to promote the construction of high performance apartment buildings within the City. Originally crafted as a targeted tax credit that encouraged the development of these apartments within areas that otherwise would not see such construction, the importance of increasing the City's stock of market rate rental housing was deemed significant enough to expand that credit to be Citywide, albeit at a somewhat reduced credit amount. However, the potential conflict with the City's Historic tax credit was recognized when the program was expanded beyond the original targeted areas. Language was included requiring High Performance Market Rate Rental Housing projects that qualified for the Historic credit to pursue it, rather than the Citywide apartment credit. However, certain eligibility criteria created a hindrance to this effort. The language in the proposed legislation would resolve this issue.

To be clear, it should be noted that this change will not affect those High Performance Market Rate Rental Housing projects that fall under the original Targeted tax credit, which does not currently exclude properties that qualify for the Historic tax credit. In light of this limitation, the Finance Department believes the additional oversight provided by a CHAP review of projects that would otherwise be receiving the Citywide High Performance Market Rate Rental Housing Projects over \$3.5 Million can only benefit the City.

Recommended Compliance and Enforcement Amendments

The continued success of the Historic Tax Credit program is a goal shared by all of the stakeholders involved with the credit. However, as the credit continues to grow in popularity, the Department of Finance understands the growing need to prevent abuse of the credit and provide both additional oversight and more reliable enforcement options. To that end, the Department proposes one additional amendment (#2) to the proposed legislation.

Penalties for Fraudulent Applications

The proposed amendment takes enforcement to the next step and targets those credit applicants and recipients that attempt to defraud the City. There is currently no prescribed enforcement tool to both deter fraudulent tax credit applications and to punish those caught engaging in such behavior. For that reason, the Department of Finance proposes that the following language, found in attached amendment #3, be added to Subtitle 10 of Article 28 of the City code:

Any person who knowingly violates any provision of this subtitle or any rule or regulation adopted under this subtitle is guilty of a misdemeanor and, on conviction, is subject to a fine of not more than \$1,000 or to imprisonment for not more than 12 months or to both fine and imprisonment for each offense, unless the penalty listed in the Section is less, in which case that penalty governs.

This amendment will provide additional enforcement authority and help to ensure that the City's tax credits continue to be administered in a prudent and responsible manner while those that would attempt to steal from the City are appropriately punished.

Fiscal Impact

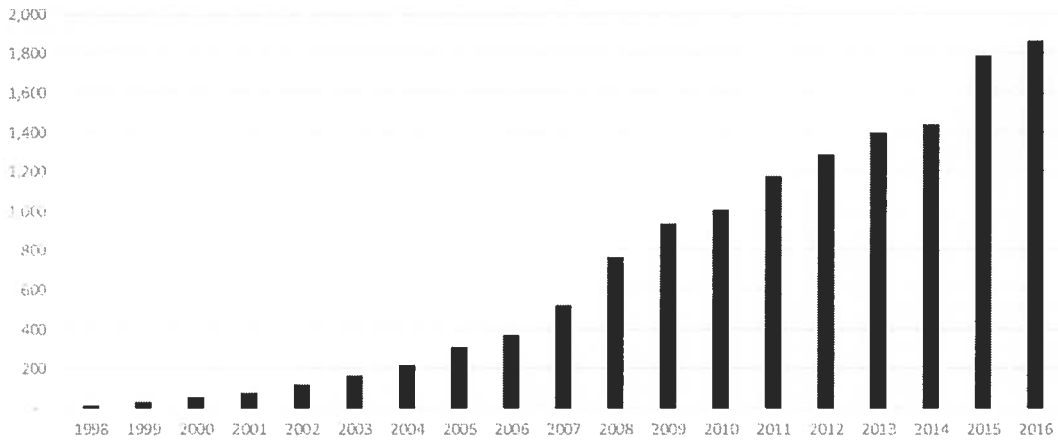
The Department of Finance recognizes the many positive outcomes achieved by the Historic Tax Credit. However, these outcomes come with a well-defined cost. For every historic restoration that is undertaken and receives the tax credit, the City forgoes taxes on the increased value of the property attributable to the improvements made. While the City has deemed the benefits of this tax credit program to outweigh the costs, any expansion of the credit should be given significant consideration in light of the City's current financial situation and how much the tax credit's usage has exploded in recent years.

HISTORIC TAX CREDIT GROWTH OVER 5 YEAR PERIODS

<u>FISCAL YEAR</u>	<u>NEW HISTORIC CREDITS</u>	<u>TOTAL NUMBER OF ACTIVE CREDITS</u>	<u>% GROWTH IN TOTAL ACTIVE CREDITS</u>	<u>TOTAL CREDIT COST</u>
2006	60	375	7.8%	\$ 2,648,073
2007	148	523	39.5%	\$ 3,826,536
2008	260	767	46.7%	\$ 5,330,463
2009	205	937	22.2%	\$ 6,251,416
2010	123	1,004	7.2%	\$ 7,306,919
New Credits Issued between 2006 and 2010				796
Total Credit Cost between 2006 and 2010				\$ 25,363,405
Average Cost per year between 2006 and 2010				\$ 5,072,681
2011	248	1,174	16.9%	\$ 8,363,415
2012	231	1,286	9.5%	\$ 8,339,549
2013	280	1,397	8.6%	\$ 7,159,296
2014	260	1,436	2.8%	\$ 7,078,187
2015	664	1,785	24.3%	\$ 8,680,914
New Credits Issued between 2011 and 2015				1,683
Total Credit Cost between 2011 and 2015				\$ 39,621,361
Average Cost per year between 2011 and 2015				\$ 7,924,272

As the chart above indicates, the City has issued twice as many Historic tax credits in the last five years as were issued in the preceding five year period. Given the increase in volume, it comes as no surprise that the Historic tax credit has cost the City, on average, \$2.9 million, or 58% more per year over the last five years than the previous five year period. FY2015 alone saw the City issuing 664 new Historic tax credits and facing a total Historic tax credit cost of \$8.68 million, a number projected to grow to over \$9.50 million in FY2016. This growth in the overall cost and usage of the credit demonstrates the clear risk associated with any expansion of this credit's benefits.

TOTAL NUMBER OF HISTORIC TAX CREDITS AWARDED



In particular, the Department of Finance would like to stress the large potential impact of the increase in the allowable construction costs under the full credit. Between FY2000 and FY2016, a total of eighteen (18) projects received the “over \$3.5 million” version of the Historic Tax Credit. Twelve (12) of these projects are still active as of FY2016.

Based upon the Project Budget submitted by the applicants, four (4) of these active properties would not have reached the proposed \$5.0 million threshold. Had these four (4) properties been approved at the 100% credit amount, the properties would have collectively received \$2.57 million more in tax credits over the 10-year term of the credit. The Department of Finance does not believe that a need exists to expand the current limitations of the Historic Tax Credit, especially during a period in which the City is experiencing fiscal stress.

The Billing Integrity Unit has also examined several potential cases of fraudulent activity. However, with no current legal framework to pursue prosecution, these investigations have proved futile. The penalties established by the Department’s third amendment are likely to generate additional savings through the discouragement of fraudulent activities in addition to providing an incentive to pursue criminal charges against those individuals determined to have acted fraudulently.

The Department of Finance supports CCB 15-0585 with the included amendment.

CC: William Voorhees
David Ryker
Natawna Austin

Department of Finance Proposed Amendments to CCB 15-0585

Amendment #1

On page 2, in lines 9 and 11 of the proposed legislation strike the brackets surrounding \$3.5 and strike the \$5 appearing immediately thereafter, having the effect of returning the amount of construction costs above which a credit limitation is enforced to \$3.5 million.

9 (f) *Amount of credit – Limitation on projects more than ~~3.5~~ \$5 million in construction*
10 *costs.*

11 (1) For development projects exceeding ~~3.5~~ \$5 million in documented construction
12 costs, the tax credit is limited to the following percentages of the amount computed
13 under subsection (e) of this section:

14 (i) in years 1 through 5 - 80%

15 (ii) in year 6 - 70%

16 (iii) in year 7 - 60%

17 (iv) in year 8 - 50%

18 (v) in year 9 - 40%

19 (vi) in year 10 - 30%.

Department of Finance Proposed Amendments to CCB 15-0585

Amendment #2

On Page 3, prior to the existing line 10 insert the following language:

§§ 10-31 to 10-39 {RESERVED}

§ 10-40 PENALTIES

ANY PERSON WHO KNOWINGLY VIOLATES ANY PROVISION OF THIS SUBTITLE OR ANY RULE OR REGULATION ADOPTED UNDER THIS SUBTITLE IS GUILTY OF A MISDEMEANOR AND, ON CONVICTION, IS SUBJECT TO A FINE OF NOT MORE THAN \$1,000 OR TO IMPRISONMENT FOR NOT MORE THAN 12 MONTHS OR TO BOTH FINE AND IMPRISONMENT FOR EACH OFFENSE, UNLESS THE PENALTY LISTED IN THE SECTION IS LESS, IN WHICH CASE THAT PENALTY GOVERNS.