metropolitan washington
COUNCIL OF GOVERNMENTS
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December 11, 1991

Mr. Ken Gervais
METRO
2000 SW First Avenue
Portland, Oregon 97201-5398

Dear Mr. Gervais:

Per your request, please find enclosed the information you requested on the Montgomery County residential and commercial excise tax.

Should you have any questions or need additional information, feel free to contact me or José F. Bright, my Executive Assistant.

Sincerely,

Ruth R. Crone
Executive Director

Agenda Item 4
December 3, 1991

MEMORANDUM

TO: County Council

FROM: MF Michael Faden, Senior Legislative Attorney

SUBJECT: Final Action: Bill 34-90, Excise Tax - Construction

Bill 34-90, Excise Tax - Construction, sponsored by Council President Leggett, Council Vice-President Adams, and then-Councilmember Potter was introduced on March 13, 1990. A public hearing was held on April 19, 1990. On April 27, 1990, the Council voted 4-3 not to consider Bill 34-90.

The Council held another hearing on Bill 34-90, and other revenue measures, on April 2 and 4, 1991. The Management and Fiscal Policy Committee held a worksession on Bill 34-90 on April 16, and recommended that the bill pass with amendments. At a worksession on May 14, the Council adopted a number of amendments. On September 24, the Council voted to defer action on Bill 34-90 until December 3, to allow time to consider the relationship of potential development district legislation to this bill. On November 26 the Council discussed a proposal from the Executive branch for an approach to infrastructure funding that included development districts and the construction excise tax, and informally directed the Executive branch to proceed with the drafting of appropriate legislation.

Council amendments

This section of the memo will describe the amendments adopted by the Council at its May 14 worksession.

Rates The Council adopted the following rate schedule ($ per square foot of gross floor area):

Single-family Residential	**$3.75**
Multi-family Residential	**$3**
Warehouse, Manufacturing, Research and Development, and Nonprofit Office	**$2.40**
Other non-residential (e.g. office, retail)	**$4**
Nonprofit care-giving facilities, private schools	**$1**

For most categories, these rates are lower than the rates recommended by the Executive and the MFP Committee.

Exemptions The tax will not apply to the first 1200 square feet of any building, and to the first 1200 square feet of each dwelling unit in a multi-family building. The Council rejected the MFP Committee recommendation for a graduated scale of exemptions for multi-family dwelling units based on the number of bedrooms in the unit.

Also exempted are buildings used primarily for religious activities and Moderately Priced Dwelling Units, Productivity Housing Units, and similarly price- and rent-controlled housing units.

"Gross Floor Area" The Council redefined "gross floor area" -- the standard of measurement by which the tax is applied -- to include all enclosed spaces in a building except:

-- unfinished basements or attics with less than 7'6" headroom;

-- interior amenity spaces that are required for site plan approval;

-- the "upper floors" of atria and other multi-story spaces;

-- parking garages; and

-- accessory structures that are not separate buildings (e.g. decks, loading docks).

Time of payment The Council decided that 50% of the tax must be paid at occupancy (in a building with multiple stages of occupancy, issuance of the first occupancy permit). The MFP Committee had recommended that 100% be paid when the building permit is issued. Since the May worksession, the Executive has changed his position and now supports 100% payment at occupancy, so the Council may revisit this issue (see Issue 6).

Effective dates The tax will apply, at 50% of the full rates, to buildings with permits issued on or after April 1, 1992. The full rates will apply to buildings with permits issued on or after April 1, 1993. The tax will expire on June 30, 1996.

Issues

1) Will this tax produce enough revenue, at the rates proposed, to achieve its purpose?

Under the Executive's infrastructure funding proposal outlined on November 26, the construction excise tax is intended to fund needed transportation capital projects outside the development districts. Inside the development districts it would be replaced, at least partially, by a development impact excise tax targeted to the particular area. The latest revenue estimates prepared by OMB (circle 62-64), based on the Planning Department's intermediate construction forecast, show that this tax will raise about $13 million a year when it is fully effective. Of that, the first $5 million is dedicated to the Housing Initiative. If anything, OMB's estimate may be high because it assumes only 15% of the total revenue will be lost to credits for the impact taxes in Germantown, Eastern Montgomery County, and Shady Grove (if enacted), while in our view more than 15% of the total construction in the County will probably occur in those 3 areas.

The Council's previous discussions evaluated the tax's rates almost exclusively in terms of impact on developers and the housing market. These factors are of course legitimate, but up to now the Council has not focused on any specific revenue goal as distinct from generally augmenting the County's ability to fund infrastructure. The Executive's infrastructure funding proposal suggested a goal against which this tax's projected yield could be measured. Assuming the Council agrees with this goal, the question then becomes: does the projected yield -- very roughly, about 30% of the annual cost of transportation debt service in FY 1992 or 50% of the annual roads and bridges CIP during the next 6 years -- represent the share of Countywide transportation capital costs that new development should directly pay? If so, the proposed rates are adequate. If not, the rates should be adjusted either upward or downward. (The Council can revise the rates of this tax after it is enacted as well as before. See circle 4, lines 8-10.)

The Executive would prefer to reinstate the original higher rates, and lower them if the legislature gives the County its own gas tax or another way to pay for improved transportation infrastructure. (See memo, circle A1.) See also West*Group's letter, circle 50, arguing for reduced rates on competitiveness grounds.

2) Should nonprofit nursing homes and life-care centers be taxed as housing or as caregiving facilities? Or be exempt from the tax?

Under the rate structure approved at the May worksession, we understand that the construction of a nonprofit nursing home would be treated as a caregiving facility and taxed at $1 per square foot, but a profit-making nursing home or a residential life care community would be taxed at the residential rate of $3 a square foot. Does this match the Council's intention? If so, we will either clarify the bill or see that the minutes and legislative history reflect this intention.

A continuing care retirement community has proposed that such developments be exempt from the tax altogether (Strawbridge Run letter, circle 59). Should these communities be grouped with low- and moderate-income housing as exempt classes? Since continuing care communities tend to charge high rates and serve affluent populations, staff does not recommend this exemption.

3) Should buildings used for higher education be exempt from the tax?

Johns Hopkins University complains that it would be placed at a further competitive disadvantage to the University of Maryland and other public higher education institutions if it has to pay the excise tax, even at the $1/square foot rate that applies to nonprofit educational institutions. (See letters, circle 52.) Councilmember Hanna would exempt them, Columbia Union College, and any other future private post-secondary institutions by inserting the following after circle 6, line 8:

(f) a building or part of a building owned by an accredited college or university and used exclusively for instruction, instruction-related research, and administration of higher education programs;

This clause would exempt classrooms, academic research laboratories, and academic administration offices from the excise tax, but would not exempt private office buildings that happen to be owned by a university.

The arguments for exempting private universities are set out in the Johns Hopkins and High Technology Council letters. The counterargument might be that private elementary and secondary schools (and for that matter, private day care centers and other human service facilities) serve similar public functions, and yet they are taxed under Bill 34-90, so why should higher educational institutions be exempt? Is it simply because they are more prestigious, or do higher educational institutions bring more tangible or indirect economic benefits?

4) Should replacement buildings be exempt from the tax?

Reconstruction and alteration of existing buildings is exempt from the tax (circle 5, lines 10-12). Attorney Harry Lerch asked whether this exemption would cover replacement buildings -- that is, when an old building is torn down and a new one built in its place, with no additional square footage.

Staff's view is that the exemption as written does not cover this situation. Should the exemption be broadened to cover replacement buildings that do not exceed the size of the demolished building? If so, should it also exempt that part of a larger replacement building that is equal to the square footage of the demolished building?

Mr. Lerch argues that the law governing APFO treatment of loophole properties allows similar treatment of replacement buildings, and that a new building will bring in more sales and income tax revenue. Allowing this exemption might provide an incentive to upgrade existing business districts, but it also would favor some commercial construction at the expense of others. If the Council approves this exemption, in our view it should be limited to buildings that receive a construction permit not more than 6 months after the previous building is demolished.

5) Should credits against this tax be allowed for other taxes or private expenditures?

A) Introduction

Under Bill 34-90, credits would be allowed for amounts paid for other taxes that in some way duplicate the construction excise tax. The Council did not discuss this issue at the May 14 worksession. The Management and Fiscal Policy Committee bill includes the following:

[[52-49]] 52-62. Credits.

Any person who must pay the tax levied under Section [[52-47]] 52-60 may reduce the tax due by:

(a) any amount the person paid under [[Section 52-]] Article VII (development impact tax) for the building that is the subject of this tax; and

(b) any amount the person paid or is required to pay for any development district tax levied under County law, to the extent that the development district tax is in addition to (and not a part of or substitute for) the ad valorem real property tax levied on the building that is the subject of the tax under Section 52-60.

The first credit allowed, under §52-62(a), is for the development impact tax now levied in Germantown and Eastern Montgomery County. The developer could deduct the amount of impact tax paid from whatever it owes for the excise tax, and would pay any additional amount due for the excise tax. In effect, the developer pays the higher of the two taxes.

The Committee inserted §52-62(b) on Councilmember Hanna's motion to establish the principle that a credit should be allowed for a development district tax. Committee Chair Praisner preferred to see what kind of development district tax is enacted before approving a credit for it. Staff drafted subsection (b) to exclude development district taxes that are property taxes or substitutes for the property tax, such as the tax levied in a tax increment financing district created under state law [Art. 41, §14-201 et seq], because the County cannot adopt property tax credits without express state approval and this credit could be construed as a direct or indirect property tax credit.

Developers have argued that credits should also be allowed for other expenditures required by the County or paid to build a project faster, such as "road club" payments and traffic mitigation expenses. The MFP Committee discussed this issue extensively and expressed interest in a broader set of credits, but specified only those credits mentioned above. The Executive supports a credit for the development district tax but prefers to adopt it when that tax is enacted, and does not support other credits. (See Executive's July 12 memo, circle A1.)

B) Possible criteria

Allowing credits for other taxes, not to mention private expenditures, would potentially sacrifice much of this tax's revenue yield. It also raises questions of equity that involve the reasons for enacting this tax -- that is, whether this excise tax is intended to pay for only specific infrastructure items as the impact tax was, or whether it is intended to cover broader costs of growth as well.

In deciding whether to allow a credit against the construction excise tax for another tax paid (e.g. a development district excise or impact tax) or for a direct private expenditure (e.g a road club), staff proposes the following criteria:

a) Does the other tax or expenditure fund the <u>same infrastructure needs</u> (e.g. roads, schools) as the construction excise tax does? If the other tax or expenditure pays for the same kind of projects, a credit against the construction excise tax may be justified.

b) Does the construction excise tax pay the <u>full cost</u> of the infrastructure needs it funds? In other words, would the other tax (e.g. a development district tax) or private expenditure replace only the construction excise tax, or would it also replace revenues from the property and income taxes? If the other tax would shift costs from the property or income taxes, a credit against the construction excise tax probably is not justified.

c) Does the payer of the other tax or private expenditure receive a <u>special economic benefit</u> (e.g. faster development, higher density, APFO compliance) for paying it? If so, a credit probably is not justified.

C) Private expenditures — special issues

In applying the "special economic benefit" test to <u>non-tax expenditures</u>, a distinction might be made between payments to the County for the basic right to develop a property and those made to move a project to completion earlier. The developer expenditures <u>necessary to develop a property</u> include permit application and other fees, site plan implementation costs (e.g. internal roads, stormwater ponds), stormwater management fees, and land dedications (e.g. school sites, parks). Often land dedications and site plan requirements do not result in any loss of density for the developer. Developer expenditures that are not legally required to develop a property, but which <u>make possible earlier development</u> than would otherwise be allowed under the Annual Growth Policy staging ceilings, include local area and policy area improvements such as offsite road mileage, intersection improvements, or traffic mitigation programs.

In our view, the latter class of expenditures implement the developer's business decision to invest funds "up front" in order to build a project sooner. As someone said, "The developer pays the County instead of the bank." However, these expenditures do benefit the public as a whole by improving transportation capacity for everyone; even if a road is required to serve a particular development, it is of course not used only by that development's occupants. By the same token, other residents also suffer from the effects of that development and that road: congestion, noise, air pollution, among others.

D) Partial credits?

Finally, the Council might ask: Should any credit be allowed on a dollar-for-dollar basis? In other words, should a credit be given for 100% of the other tax paid, or only for part of that payment (e.g. 50%)? A lower credit may be especially valid for private expenditures, where the County has no direct control over the amount spent and so might want to give the developer an incentive to limit costs. If credits for private expenditures are allowed, the County should also be prepared to audit those expenditures closely to confirm that unnecessary or unrelated costs are not included in the claim for credit.

Perhaps a fair solution (or an uneasy compromise) would be to allow a partial credit — say 33 or 50% of the developer's out-of-pocket expenditures — for voluntary contributions that underwrite the County's infrastructure needs. For an expenditure to be credited, the infrastructure item should be in the strategic plan approved by the Council, to be sure that it is needed in the relatively near future.

E) Relationship to impact tax credits

A related issue is: **Should the credit under the existing impact tax law for building an impact highway be transferable to the excise tax?** Under the impact tax law, a developer who builds all or part of an offsite road that is on the list of roads to be paid for by the impact tax receives a dollar-for-dollar credit for its expenditures, up to the amount of the impact tax due. The question then becomes: should the applicant receive a credit under the excise tax for only the amount of impact tax actually paid, or also for the amount spent on a road and credited against the impact tax?

This is a difficult issue because either result — allowing the credit or denying it — will treat similarly situated developers differently because of the accident of their property's location either inside or outside an impact tax district. The ideal solution would be to repeal the impact tax entirely and let the excise tax replace it, but the County Attorney believes that repealing it will weaken our defense against lawsuits attempting to recover previously-paid impact fees. We would recommend that the impact tax credit be transferable only to the extent that a developer outside the impact tax areas who contributes to a transportation improvement will also receive a credit for its similar expenditure. In our view, this best achieves (albeit imperfectly) the goal of equal treatment of developers Countywide.

6) Should the time for payment of the tax be moved to the issuance of the occupancy permit?

At the May worksession, the Council decided to make 50% of the tax payable at building permit issuance and the remaining 50% at the issuance of the first occupancy permit, or before the final inspection for buildings that do not receive occupancy permits. The original bill had required the entire tax to be paid when the building permit is issued, and developers strongly objected that up-front payment would pose a hardship to them because they receive no revenue (except construction loans) at that time. The Executive had opposed the change to 50% payment at occupancy.

Now the Executive has proposed (see July 12 memo, circle A1) that the entire tax be paid at occupancy. This would postpone the receipt of 50% of the revenue for, on average, a year or more. This change would not affect the amount of tax collected, because that is determined when the building permit is issued (or applied for; see next issue). If the developer does not pay the tax, the County could attach a lien to the property, so we don't see many tax collection problems stemming from this postponement. However, some revenue could be lost when developers who would have paid half of the tax when the building permit is issued don't complete their projects. The issue here is mainly whose cash flow needs should be served, the County's or the developer's.

7) Should the tax be triggered by the filing of a completed application for a building permit, instead of the issuance of the permit?

The version of Bill 34-90 before you makes this tax take effect for construction for which a building permit is issued on or after April 1, 1992. DEP prefers to have the tax triggered by the filing of a completed permit application; that will relieve pressure on them to issue a permit too quickly. They assure us that disputes over when an application is complete are not common. (Also see Lerch letter, circle 61.) Bill 34-90 as introduced took this approach, but staff had recommended that issuance of the permit be used so as to reduce potential litigation about when a given application was complete.

If this change is made, the Council should also consider advancing the effective dates from April 1, 1992 and 1993. Moving the trigger point from permit issuance to filing of an application would as a practical matter delay the application of the tax to a given building by about 3-6 months. If the Council wants to tax the same buildings that would pay under the current draft, the effective dates should be no later than January 1, 1992 and 1993. (However, see the next issue.)

In a related issue, the Planning Board has questioned whether those projects that received 6-month building permit extensions under Bill 27-91, which the Council enacted in July, should somehow be made subject to the tax. In our view, those projects should be covered only if their current building permit lapses and they have to apply for a new one; this is similar to the way such projects are treated for APF purposes.

8) Should economic indicators be used to determine when the tax should take effect?

Councilmember Praisner has proposed an amendment (circle B1) that would base the initial effective date of this tax on the achievement of a real estate recovery, as measured by certain economic indicators. (See background on indicators, circles B2-B4.) The Executive could modify the trigger points or substitute new indicators by a method 1 regulation, which is subject to Council approval.

The questions this amendment poses are:

-- Is this approach conceptually sound? Shouldn't the tax cover all construction as long as the funds are needed, instead of waiting until the real estate markets reach certain points? Any new construction arguably is, by the fact of its existence, economically able to contribute its share of infrastructure funding. The counterargument is that imposition of the tax before a recovery gains momentum will stifle investment; thus this approach triggers the tax when the market will bear it. A related concern is whether developers are more damaged by uncertainty and unpredictability in their financial planning; they can pay this tax, the argument goes, as long as they know about it long enough in advance.

-- If this approach is sound, are these the best indicators? Is the data they rely on accurate and timely? Councilmember Praisner has expressed an openness to alternative suggestions.

9) Administrative issues raised by the Executive's most recent memo:

a) Basements DEP expects a certain amount of tax avoidance by builders selling a house with an unfinished basement and then finishing it after the tax is paid. They propose taxing all basements at half their measured square footage. Staff is not sure this is necessary because the exemption for unfinished basements and attics exempts only those with headrooms lower than the minimum allowed in the Building Code; thus any exempt basement cannot legally be finished for human occupation. (Of course, many are anyway.)

b) Garages Louis D'Ovidio's memo argues that exempting garages gives an unfair advantage to buyers of larger houses. He may be right, but we agree with the Executive that it is too late in the process to change this.

c) Cost of Administration Staff agrees with the Executive that the cost of administering this tax should be taken from the tax itself. OMB estimates this cost at $350,000 the first year and $100,000 each later year. We included in the latest redraft an amendment to cover these costs (circle 9, lines 21 et seq).

Revenue Estimate

For the most recent revenue estimates from OMB, see circle 62.

This packet contains:

1229 LAW 65

Montgomery County Government
ROCKVILLE, MARYLAND 20850

Neal Potter
County Executive
(301) 217-2500
TTY 217-6505

MEMORANDUM

July 12, 1991

TO: Isiah Leggett, President, Montgomery County Council

FROM: Neal Potter, County Executive NP

SUBJECT: Bill 34-90, Construction Excise Tax

I appreciate the progress the Council has made on refining the Construction Excise Tax (CET). After reflecting on Council changes, I have some additional recommendations.

1. Rates and Revenue

The Council has tentatively reduced the tax rate on apartments from the $3.75 per sf that I recommended to $3.00; office and retail from $5.00 to $4.00; and warehouse, manufacturing, and R&D from $3.00 to $2.40. These lower rates will reduce revenue proportionately. I believe it would be more prudent to establish initially the higher rates I recommended, but with the understanding that the lower rates would be substituted if the State Legislature grants the County an additional way to tax vehicles to pay for improved transportation infrastructure.

2. Basements

The Council tentatively voted to tax the finished area of occupiable basements, rather than the total area as earlier proposed. Construction Codes staff informally estimate that about 50 percent of detached houses and 70 percent of townhouses are sold with finished basements. Also, when a basement is finished, about 80 percent of the area is finished; the remainder is utility, laundry, etc.

Construction Codes staff believes that builders and homebuyers will respond to a tax on finished area only by making the sale with an unfinished basement and arranging for completion of the basement after occupancy. This response could be avoided by a uniform approach of taxing just half of the basement area, whether finished or not. The revenue result to the County would be similar to the Council's intent, evasion would not be encouraged, and the administration of the tax would be simpler.

3. Garages

Recently, I shared with you a memo from Lou D'Ovidio in which he raised a question about exempting house garages and argued for taxing them. Upon reflection, I recommend that this point not be pursued at this time. The existing development impact tax in Germantown and Eastern County does not tax garages, the exemption for garages was included in the bill as advertised, and all subsequent discussion with the homebuilders has assumed this exemption. Although the Council and I are not precluded from considering this new issue, I recommend that we complete action on the bill within the parameters previously defined.

4. Paying for Housing and for Tax Administration

The Council has revised the bill to provide that the first $5 million in revenue each year from the construction tax be assigned to the Housing Initiatives Fund. I question whether this reservation is in line with the basic purpose of the tax, which is to have new construction pay a share of the cost of infrastructure to serve it.

In addition, I hope the Council will consider a clarification to allow a deduction for the cost of collection and administration before the set-aside for infrastructure or other designated use restriction. The Council and I are faced with a choice of paying for these collection costs either from the General Fund or from the construction tax revenues.

Particularly in FY 92, Finance and Construction Codes will have some setup costs for information systems and there will be an ongoing staff cost. It is reasonable to charge the cost of collection against the revenue from a tax and it is particularly important in current fiscal circumstances not to place burdens on the General Fund when there is a reasonable alternative.

Rather than have the collection costs be charged to other General Fund revenues, I recommend that the bill allow those costs to be deducted before the revenues are assigned to an infrastructure (transportation) fund (or the Housing Initiatives Fund, if that is the Council's decision).

5. Payment at Building Permit Approval

Executive and Council staff met with representatives of Rockville and Gaithersburg to request their cooperation in the collection of the tax from applicants for municipal building permits. While municipal staff stated their willingness to calculate and collect the tax, they have stated that the administrative burden would be such as to require that the entire tax be collected at the time a building permit is issued.

The administrative complexity of collecting the tax at two points in time coincides with the underlying concern for construction financing and the industry impact of collecting this tax prior to any realization of proceeds from construction. I am therefore changing my recommendation as to when we should collect the Construction Excise Tax and would now request that Council approve its collection *in full at time of settlement*, for residential units, and *upon issuance of certificate of occupancy*, for commercial construction. This will significantly reduce the complexity and work involved for County departments, and will most correctly impose the tax at the point in time where a cash transaction takes place.

6. <u>Credit for Development District Tax</u>

In a memo to the Council on the Shady Grove master plan, I am recommending that we proceed with a development district for Shady Grove. Staff is also working on a development district analysis for Germantown. There are a range of options for financing capital and operating costs in a development district, but I am recommending at this time a particular approach. I believe that the following is simple and workable:

a. The development district should pay for all of the transportation capital improvements not normally the responsibility of the developer. The County would pay for other community facilities not negotiated through special circumstances such as optional method of development.

b. The development district should cover capital costs with a development impact excise tax (DIET). Developers should have the option to pay most of the DIET over a period of years, with the unpaid balance due at any transfer of the property.

c. Credit against the construction excise tax should be given for the DIET.

d. Operating costs for special levels of service in a development district may be covered by a property tax, like an urban district. However, if a parking fee or tax can be made workable within the district, then it would be preferable to a property tax.

This approach is consistent with the preference of the Council for a credit against the CET for any development district impact tax. I can support the credit with the understanding that the district tax would cover all of the transportation capital projects.

Although I am now supporting the credit, I still recommend that you include the credit in your action on a development district bill, rather than to include it also in Bill 34-90.

NP/sa

Bill 34-90 Construction Excise Tax

Amendment by Councilmember Praisner

Effective date — economic indicator triggers

Add at end of §2(a) on circle 10, line 25:

However, the tax does not apply until the first day of the next month after the Director of Finance certifies that:

(1) the number of housing unit completions in the County during the most recent 12 months for which data are available exceeded 50% of the average annual number of housing unit completions during the preceding 10 years;

(2) the number of taxable residential real estate transfers in the County during the most recent 12 months for which data are available exceeded 50% of the average annual number of taxable residential real estate transfers during the preceding 10 years; and

(3) the amount (measured in square feet) of non-residential space completed in the County during the most recent 12 months for which data are available exceeded 50% of the average annual amount of non-residential space completed during the preceding 10 years.

The Executive may, by Regulation adopted under method (1), modify the percentage amount of any of these criteria or substitute new criteria.

B-1

MONTGOMERY COUNTY
HOUSING COMPLETIONS
1960–1990

Year	No. of Units
1960	4,033
1961	5,289
1962	5,813
1963	5,042
1964	5,792
1965	6,751
1966	10,445
1967	8,854
1968	7,046
1969	6,806
1970	4,162
1971	6,640
1972	7,484
1973	8,468
1974	6,156
1975	2,281
1976	2,042
1977	3,213
1978	3,224
1979	3,855
1980	4,979
1981	4,879
1982	3,506
1983	6,153
1984	8,400
1985	9,761
1986	10,364
1987	9,824
1988	8,435
1989	5,514
*1990	3,081
Total	188,292

* Preliminary Estimate

B-2

	Data Availability	Actual 1985	Actual 1986	Actual 1987	Actual 1988	Actual 1989	Actual 1990		Actual/ Est. 1991	Estimated 1992	Estimate 1993
HOUSING VALUES											
RESALE SINGLE FAMILY - MONT. CO. (Jarchow) MEDIAN	Not Available	$93,835	$103,220	$116,640	$130,800	$150,600	$148,880	Data no longer available			
BOARD OF REALTORS											
MEDIAN - SINGLE FAMILY	Monthly					$167,000	$160,000	YTD thru Sept. $169,900, 0.5% below same period last year.			
AVERAGE -	Monthly					$219,543	$202,650	YTD thru Sept. $200,282, 0.1% below same period last year.			
SALES VOLUME	Monthly					9,794	7,955	YTD thru Sept. 8,580 sales, up 4% from 8,208 last year.			
FHFB - AVERAGE PURCHASE PRICE - WASHINGTON AREA	Quarterly	$152,600	$156,600	$159,500	$180,400	$196,000	$202,400	Thru first three quarters of 1991, $225,900			
NUMBER OF TAX. REALTY TRANSFERS	Monthly	20,185	22,519	20,190	23,759	22,516	18,666	First four months of FY 92 5,848/5,560	15,243	18,925	17,500
AVG. TAX PER TRANSFER	Monthly	$1,396	$1,594	$1,595	$1,963	$2,297	$2,344	First four months of FY 92 $2,297/$2,210	$2,250	$2,340	$2,435
AVG. TAX PER RES. TRANSFER (Impr. Res. Valued over $70,000)	Monthly	$1,172	$1,288	$1,354	$1,635	$1,870	$2,099	First four months of FY 92 $2,132/$2,118	$2,095	$2,179	$2,270
NEW CONSTRUCTION ($ Mil.)											
NEW CONSTRUCTION - MONT. CO. (Valuation of ALL permits)	Monthly	$836.4	$883.0	$896.3	$826.4	$729.5	$598.7	First 9 months of FY 92 $387.5 mil./$503.2 mil.			
New Residential Bldgs.	Monthly		$399.4	$420.0	$350.4	$379.9	$286.0	$163.9 $254.1			
New Stores	Monthly		$24.4	$29.0	$32.3	$14.7	$25.2	$8.6 $23.2			
New Office, Bank Bldgs.	Monthly		$191.3	$165.0	$150.8	$86.5	$32.3	$18.5 $26.5			
								Sept. 1991 shows 0.4% gain over Sept., 1990		Est.	Est.
NEW CONSTRUCTION ADDED TO ASSESSABLE BASE Amount (Fiscal Year)	Quarterly	$330.2	$588.0	$660.1	$668.4	$637.8	$592.1	3/4 Year Levy yielded $99.0 mil. in base 73% above the $57.2 mil. last year (Montgomery Mall)	$405.0	$360.0	$275.[illegible]
Percent Change from Previous Yr.		37.1%	78.3%	12.1%	1.0%	-4.3%	-7.2%		-31.5%	-11.3%	-23.[illegible]
OFFICE/R & D SPACE											
NEW SPACE DELIVERED Sq Ft.	Half Year	3.1 Mil.	2.85 mi	2.45 mil	1.5 mil	2.37 mil	1.1 mil	OED estimates approximately 175,000 sq ft. for all of 1991.			
NEW SPACE ABSORPED Sq Ft.	Half Year	1.73 Mil.	2.57 mi	2.49 mil	1.7 mil	2.06 mil	1.19 mil	OED expects absorption to total just over 600,000 sq. ft. in 1991.			
VACANCY RATE %	Half Year	9.9%	10.5%	10.5%	10.9%	12.6%	12.7%				
RETAIL SALES											
TOTAL RETAIL SALES S&MM ($ mil.) Montgomery County	Annual	$5,530	$6,053	$6,468	$6,883	$6,301	$6,575	S&MM estimates total retail sales in 1995 of $7.52 bil.			
Percent Change from Prior Yr.		8.27%	9.46%	6.86%	6.42%	-8.46%	4.35%	Methodology change in 1989			
STATE SALES AND USE TAX COLLECTIONS (Fiscal Years) Montgomery County ($ mil.)	Monthly	$172.8	$186.1	$207.6	$226.1	$237.3	$243.2	Sept., 1991 collections of $19.9 mil. were 4.4% above Sept., 1990.	$234,332		
Percent Change from Prior Yr.	Monthly	14.43%	7.70%	11.55%	8.91%	4.95%	2.49%		-3.65%		

Montgomery County Department of Finance November, 1991

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Table 1

Montgomery County Non-Residential Completions
Number of Square Feet by Land Use Type
1979-1989

Year	Office	Retail	Warehouse/ Industrial	Other	Total
1979	782,771	270,429	745,731	21,543	1,820,474
1980	1,754,631	438,414	389,243	283,643	2,865,931
1981	3,133,514	327,888	505,554	243,910	4,210,866
1982	1,476,705	745,720	701,414	0	2,923,839
1983	2,242,638	335,146	603,366	0	3,181,150
1984	2,358,754	837,298	1,433,319	133,396	4,762,767
1985	4,179,523	568,363	865,695	444,664	6,058,245
1986	4,820,474	935,221	859,556	398,788	7,014,039
1987	2,902,925	920,888	595,868	644,817	5,064,498
1988	1,643,710	899,924	1,301,813	159,719	4,005,166
1989*	2,581,050	612,436	1,165,468	46,143	4,405,097

Montgomery County Non-Residential Completions
Percent Distribution by Land Use Type
1979-1989

Year	Office	Retail	Warehouse/ Industrial	Other	Total
1979	43.0%	14.8%	41.0%	1.2%	100.0%
1980	61.2%	15.3%	13.6%	9.9%	100.0%
1981	74.4%	7.8%	12.0%	5.8%	100.0%
1982	50.5%	25.5%	24.0%	0.0%	100.0%
1983	70.5%	10.5%	19.0%	0.0%	100.0%
1984	49.5%	17.6%	30.1%	2.8%	100.0%
1985	69.0%	9.4%	14.3%	7.3%	100.0%
1986	68.7%	13.3%	12.2%	5.7%	100.0%
1987	57.3%	18.2%	11.8%	12.7%	100.0%
1988	41.0%	22.5%	32.5%	4.0%	100.0%
1989*	58.6%	13.9%	26.5%	1.0%	100.0%

* Preliminary estimate.

Note: 1. *Due to revisions in records from the State Tax Assessor's office, the volume of historical completion activity has changed from what was published in the 1989 Development Trends report.*

2. *These completion numbers do not include square feet completed in religious buildings, places of assembly, parking garages, and parks.*

Source: *Montgomery County Planning Department, Research and Information Systems Division. Compiled from revised data provided by the State Department of Assessment and Taxation. Revised April, 1991.*

TABLE 2

AMOUNT OF TAXES AND EXACTIONS LEVIED OR IMPOSED BY COUNTIES ON NEW DEVELOPMENT IN THE WASHINGTON METROPOLITAN AREA

(PER DWELLING UNIT)

	MONTGOMERY COUNTY	PR.GEORGE'S COUNTY	FREDERICK COUNTY	HOWARD COUNTY	FAIRFAX COUNTY	ARLINGTON COUNTY	LOUDOUN COUNTY
<u>County-Wide Fees</u>							
Water/Sewer "Tap" Fees	0	0	$3,000	$1,200	$6,000	$2,300	$7,400
<u>Exactions</u>							
On-Site Water and Sewer (1)	0	0	9,275	9,350	9,225	10,275	9,275
Other On-Site or Off-Site Improvements (2)	5,000	1,500	5,500	0	2,500	1,400	1,850
SUBTOTAL	$5,000	$1,500	$17,775	$10,550	$17,725	$13,975	$18,525
<u>Permitting Time</u>	4	1.5	1	1	2.5	1.5	2.5
<u>Permitting Time Cost</u> (3)	$13,500	$6,000	$ 3,000	$ 3,500	$11,000	$ 7,500	$9,000
TOTAL	$18,500	$7,500	$20,775	$14,050	$28,725	$21,475	$27,525
<u>Special District Taxes or Fees</u>							
Water/Sewer	0	0	0	$500	0	0	0
Impact Taxes or Fees	$1,489-$1855	0	0	0	$883	0	0
Property Tax Surcharge	0	0	0	0	$350	0	0

Notes: (1) All estimate based on Typical R-90 (9,000 sf) lot, 75 ft. frontage, except where noted.

(2) <u>Off-site improvements</u> are typically roads, traffic improvements, water or sewer main extensions, and off-site SWM facilities. <u>On site improvements</u> are for required improvements considered above the norm, such as the tree survey and additional stormwater management requirements in Montgomery County. Not included are those improvements that all Counties require, such as streets, storm drains, typical storm water management and sediment control, school and/or park site dedication where needed, and wetland preservation. Data reflects average of all residential development. In Arlington County, data is for high density residential units in Urban Development Areas (around metro stations); In Loudoun County, data is for negotiated development at 4 du/ac.

(3) Financing cost of holding raw land from purchase to building permit. Data reflects time from rezoning to building permit, but in Montgomery County, this holding period does not include the time to obtain rezoning if necessary. The costs shown are County-wide averages. In Montgomery County, these costs range from $2,000 for lower priced homes to over $27,000 for expensive homes.

SEE ACCOMPANYING TEXT FOR DESCRIPTION OF CATEGORIES AND COUNTIES,
AND SEE ESPECIALLY SECTION 1 FOR QUALIFICATIONS OF THIS INFORMATION

(2)

Bill No.: 34-90
Concerning: Excise Tax - Construction
Draft No. & Date: 9 9/23/91
Introduced: March 13, 1990
Expires: December 10, 1991
Enacted:
Executive:
Effective: [[September 1, 1990]] [[July]] April 1, 1992
Sunset Date: June 30, [[1996]] [[1995]] 1996
Ch. ____, Laws of Mont. Co., CY ___

COUNTY COUNCIL
FOR MONTGOMERY COUNTY, MARYLAND

By: Council Vice-President Leggett and Councilmembers Adams and Potter

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AN ACT to:

(1) establish an excise tax on persons who build or add to certain buildings, with certain effective and termination dates;
(2) set the rate of the tax, set different rates for different [[types of construction]] building use groups, and authorize the County Council to increase or decrease the rate or rates each year by resolution after notice and hearing;
(3) allow exemptions and credits, and require proof of payment of the tax before [[a building permit is]] certain permits are issued by the County or applied for in a municipality;
(4) provide for collection of the tax and payment of interest and penalties, and apply other provisions of law to this tax;
(5) designate a certain portion of the revenues from this tax for the Montgomery Housing Initiative and for other purposes; and
(6) generally amend the laws governing excise taxation of the exercise of occupations and privileges.

By adding
Montgomery County Code
Chapter 52, Taxation
Article [[VII]] VIII, Excise Tax on Certain Construction
Sections [[52-47 through 52-51]] 52-60 through 52-64

EXPLANATION: **Boldface** indicates a heading or a defined term.
Underlining indicates text that is added to existing law by the original bill.
[Single boldface brackets] indicate text that is deleted from existing law by the original bill.
Double underlining indicates text that is added to the bill by amendment.
[[Double boldface brackets]] indicate text that is deleted from existing law or the bill by amendment.
* * * indicates existing law unaffected by the bill.

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

Sec. 1. Chapter 52 is amended by adding Article [[VII]] VIII, Excise Tax on Certain Construction.

Article [[VII]] VIII. Excise Tax on Certain Construction.

[[52-47]] 52-60. Tax levied; rates.

(a) Any person who proposes to build, or add to, any building in the County must pay an excise tax on the act of engaging in the construction [[before a building permit is issued]].

(b) The rate of the tax established under subsection (a) is:

(1) $1 per square foot of gross floor area in any building or part of a building that is:

(A) owned by a nonprofit organization that is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code;

(B) intended to be used primarily for the direct provision of charitable or educational services; and

(C) not intended to be used as a [[long-term]] permanent residence;

[[(1)]] (2) $[[3.25]] [[3]] 2.40 per square foot of gross floor area in any building or part of a building that is intended to be used primarily:

(A) for [[retail sales or rental of tangible goods]] [[warehouse]] storage, industrial or manufacturing, or research and development purposes, or

(B) for offices by a nonprofit organization that is exempt from federal income taxes under Section

2

501(c)(3) of the Internal Revenue Code;

[[(2)]] (3) $[[3.25]] [[5]] 4 per square foot of gross floor area in any other nonresidential building or [[addition]] part of a building;

non-profit
< business

(4) $3 per square foot of gross floor area in any multi-family residential building or any addition to a multi-family residential building; and

multi-family
< single

[[(3)]][[(4)]]

(5) $[[3.25]] 3.75 per square foot of gross floor area in any single-family residential building, including any townhouse, or any addition to a single-family residential building.

(c) If, within 10 years after a building permit is issued, any person changes the use of all or part of a building to a use for which a higher tax would have been due under this Section when the building permit was issued (including a change from a status, use or ownership that is exempt under Section 52-61 to a status, use or ownership that is not so exempt), the owner of the building must within 10 days pay all additional taxes that would have been due if the building or part of the building had originally been used as it is later used. If the building owner does not pay any additional tax when due, each later owner is liable for the tax, and any interest or penalty due under Section 52-64, until all taxes, interest, and penalties are paid.

[[(c) On January 1 of every odd-numbered year, starting January 1, 1993, the Director of Finance must increase the rates of the tax by the percentage increase, if any, in the index of construction costs published by the United States Department of Commerce, or a similar index selected by the Director that more closely reflects costs in the Washington metropolitan area, since the tax rates were previously set. The Director must round any increase to the nearest multiple of 5 cents.]]

(d) Each year the County Council by resolution, after a public hearing advertised under Section 52-17(c), may increase or decrease the tax rate or rates set in subsection (b).

(e) As used in this [[Section]] Article, "building"[[,]] and dwelling unit[[, and "gross floor area"]] have the same meaning as in Chapter 59. "Person" includes any individual, corporation, association, firm, partnership, group of individuals acting as a unit, trustee, receiver, assignee or personal representative.

(f) (1) "Gross floor area", as used in this Article, means the sum of the gross horizontal areas of the several floors of a building measured from the exterior faces of the exterior walls or from the center line of a party wall.

(2) "Gross floor area" does not include any:

(A) unfinished basement or attic area with a clear height less than 7 feet 6 inches;

(B) interior amenity space required to obtain approval of a site plan;

(C) area occupied by an atrium or other multi-story space other than the first floor of the space;

(D) area occupied by unenclosed mechanical, heating, air conditioning, or ventilating equipment;

(E) parking garage or area; or

(F) other accessory structure that is not a separate building.

[[52-48]] 52-61. Exemptions.

The tax established under Section [[52-47]] 52-60 does not apply to:

(a) any reconstruction or alteration of an existing building or part of a building that does not increase the gross floor area of the building;

(b) the first 1200 square feet of gross floor area of:

(1) a new nonresidential building, or

(2) an addition to an existing nonresidential building;

(c) in any residential building,[[:]]

[[(1) the first 700 square feet of gross floor area in any efficiency or 1-bedroom dwelling unit,

(2) the first 900 square feet of gross floor area in any 2-bedroom dwelling unit, and

(3)]] the first 1200 square feet of gross floor area in any [[3-bedroom or larger]] dwelling unit or addition to an existing dwelling unit;

(d) (1) any Moderately Priced Dwelling Unit built under Chapter 25A,

(2) any Productivity Housing Unit, as defined in Section 25B-17(m), and

(3) 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 50% of the area median income, adjusted for family size;

[[(c)]](e) a building owned by any agency or instrumentality of federal, state, County or municipal government; or

[[(d)]](f) a building owned by a nonprofit, tax-exempt organization, used primarily for [[charitable, educational, or]] religious activities, and not used for any substantial commercial activity.

[[52-49]] 52-62. Credits.

Any person who must pay the tax levied under Section [[52-47]] 52-60 may reduce the tax due by:

(a) any amount the person paid under [[Section 52-]] Article VII (development impact tax) for the building that is the subject of this tax; and

(b) any amount the person paid or is required to pay for any development district tax levied under County law, to the extent that the development district tax is in addition to (and not a part of or substitute for) the ad valorem real property tax levied on the building that is the subject of the tax under Section 52-60.

[[52-50]] 52-63. Proof of payment.

(a) Before the Department of Environmental Protection [[issues]] releases a building permit under Chapter 8, the applicant must show that:

(1) the applicant has paid 50% of the tax due under Section [[52-47]] 52-60; or

(2) the construction is exempt from the tax due under Section [[52-47]] 52-60.

(b) Before a person applies to a city or town in the County for a building permit, the applicant must show that:

(1) the applicant has paid 50% of the tax due under Section [[52-47]] 52-60; or

(2) the construction is exempt from the tax due under Section [[52-47]] 52-60.

(c) Before the Department of Environmental Protection [[issues an]] releases a use and occupancy permit for all or any part of a building under Chapter [[8]] 59, the applicant must show that all remaining taxes due under Section 52-60 with respect to the entire building have been paid.

(d) If an occupancy permit need not be issued for a building or dwelling unit, the applicant for the inspection must show that all remaining taxes due under Section 52-60 with respect to the building or unit have been paid before the Department of Environmental Protection begins a final inspection of the building or unit.

(e) Before a person applies to a city or town in the County for an occupancy permit, or a final inspection if an occupancy permit is not required, [[of]] for a building or dwelling unit, the applicant must show that all remaining taxes due under Section 52-60 with respect to the building or unit have been paid.

[[52-51]] 52-64. **Collection; interest and penalties; violation; lien.**

(a) If any person fails to pay the Director of Finance the tax due under Section [[52-47]] 52-60, that person is liable for:

(1) interest on the unpaid tax at the rate of one percent per month for each month or part of a month after the building permit is issued; and

(2) a penalty of 5 percent of the amount of the tax per month or part of a month after the building permit is issued, not to exceed 25 percent of the tax.

The Director must collect any interest and penalty as a part of the tax.

(b) If any person fails to pay the tax [[before a building permit is issued]] when due, the Director must obtain information on which to calculate the tax due. As soon as the Director obtains sufficient information to calculate any tax due, the Director must assess the tax and penalties against the person. The Director must notify the person by mail sent to the person's last known address of the total amount of the tax, interest, and penalties. The total amount must be paid within 10 days after the notice is mailed.

(c) Every person liable for any tax under Section [[52-47]] 52-60 must preserve for 2 years all records necessary to determine the amount of the tax. The Director may inspect the records at any reasonable time.

(d) Any failure to pay the tax due under Section [[52-47]] 52-60, and any violation of Section [[52-50]] 52-63 and this Section, is a Class A violation. Each violation is a separate offense. A conviction does not relieve any person from payment of the tax.

(e) Section 52-18D applies to this tax.

(f) The Director may sign an agreement with a city or town in the County by which the city or town will collect the tax due under Section 52-60 and remit the tax to the Director. The agreement may allow the Director to pay the city or town a reasonable fee to cover its costs of collection and processing.

(g) The County Executive may adopt regulations under method (2) to implement this Article.

(h) By September 1 of each year, the Director must report to the County Council for the preceding fiscal year:

(1) the amount collected under this tax;

(2) the amount of property exempted from this tax for which [[a]] building permits [[was]] were issued; and

(3) the amount of credits granted against this tax.

(i) In each fiscal year the Director must transfer to the General Fund from the revenue received from this tax an amount sufficient to reimburse the cost of administering this tax during that fiscal year. If in any fiscal year the revenue from this tax is not sufficient to reimburse the cost of administering it, the Director must transfer the unreimbursed portion of the cost to the General Fund from the revenue received in the next fiscal year.

[[(f)]][[(i)]](i) The Director must transfer the first $5 million in revenue received each fiscal year from the tax levied under Section [[52-47]] 52-60, after transferring the funds allocated under subsection (i), to support the Montgomery Housing Initiative established under Section 25B-9. The Council must appropriate the remaining revenue to implement a strategic plan for infrastructure improvement submitted annually by the County Executive in the Capital Improvements Program, as amended by the Council. However, the Council must not appropriate more than 10% of the remaining revenue, and not more than 20% of the revenue received on account of residential construction, to the capital budget of the Washington Suburban Sanitary Commission.

Sec. 2. Effective date and expiration of law.

(a) The tax levied under Article [[VII]] VIII of Chapter 52, inserted by Section 1 of this Act, applies to any construction for which [[an application for]] a building permit is [[filed]] issued on or after [[September 1, 1990]] [[July]] April 1, 1992. The tax on any construction for which a building permit is issued on or after [[July]] April 1, 1992, but before [[July]] April 1, 1993, must be levied at 50% of the applicable rate set in Section 52-60(b).

(b) Article [[VII]] VIII of Chapter 52, inserted by Section 1 of this Act, is not effective after June 30, [[1996]]

[[1995]] 1996.

Sec. 3. Evaluation.

By October 31, [[1995]] [[1994]] 1995, the Office of Legislative Oversight must evaluate the effect of this Act.

Approved:

Isiah Leggett, President, County Council — Date

Approved:

Neal Potter, County Executive — Date

This is a correct copy of Council action.

Kathleen A. Freedman, CMC — Date

Secretary of the Council

LEGISLATIVE REQUEST REPORT

Bill 34-90
Excise Tax - Construction

DESCRIPTION:	Imposes an excise tax on the act of constructing or adding to any building in the County. The tax is measured by the size of the construction or addition (including accessory structures other than parking garages), not its cost or assessed value. The tax rate varies for different types of residential and nonresidential construction. The Council can increase or reduce the rate each year after notice and a public hearing. The tax is due before the builder receives a building permit from the Department of Environmental Protection, or when the builder applies for a building permit from a city or town in the County. Exempt from the tax are: reconstruction or alteration of existing buildings that does not increase their floor area; the first 1200 square feet of any new building or addition; buildings owned by federal, state, County, or municipal governments; and buildings owned by nonprofit organizations, used primarily for religious activities, and not used for substantial commercial activity. The taxpayer would receive a credit for amounts paid under another development impact tax. The first $5 million in revenue each year would be allocated to the Montgomery Housing Initiative.
PROBLEM:	Need for additional revenue to fund ongoing operations and new capital projects of County government, especially increased demands on public resources caused by population and employment growth in and outside the County.
GOALS AND OBJECTIVES:	To raise additional revenue in a fair and equitable manner, through means other than the property tax.
COORDINATION:	Departments of Finance, Environmental Protection
FISCAL IMPACT:	Attached
ECONOMIC IMPACT:	See attached economic impact analysis
EVALUATION:	Attached; see §3
EXPERIENCE ELSEWHERE:	Development excise tax used in other jurisdictions
SOURCE OF INFORMATION:	Michael Faden, Council staff, 217-7900
APPLICATION WITHIN MUNICIPALITIES:	Tax applies Countywide.
PENALTIES:	Class A for nonpayment or false statements; interest at 1% per month of late payment, and penalty of 5% per month of late payment (up to 25% of the tax due).

Economic Impact Statement - Bill 34-90
Excise Tax - New Construction

The Proposal

This proposal will levy a $3.25-per-square-foot excise tax on all new non-residential development, and a $3.25 per-square-foot excise tax on all residential construction. There are specified credits and exemptions including the first 1200 square feet of any new building or any addition to an existing building. The annual average revenue estimate is $30 million, using the Planning Board's 5-year intermediate forecast; this estimate will vary from year to year as well as for the Board's low and high forecasts.

The Impact

In assessing the fiscal and economic impact of this tax, there are a number of alternative approaches. This statement uses a differential tax incidence approach -- i.e., what are the effects of financing expenditures by imposing a development excise tax rather than increasing property tax rates?

The County will receive $30 million from either a 13¢ property tax rate increase or the proposed excise tax on new development. The <u>initial</u> incidence of a property tax rate increase would be 67% ($20 million) on households and 33% ($10 million) on existing non-residential properties. For the excise tax, 100% of the <u>initial</u> incidence will be on developers of new properties.

Since both households and businesses can deduct property taxes from their State and Federal income taxes, these treasuries will pay a portion of the property tax increase, at applicable marginal rates, for those who itemize deductions. The development excise tax should also be deductible for State and Federal income tax purposes; thus, some of that burden is also transferred to those levels of government.

For the residential portion of the property tax increase, after income taxes, the incidence would be totally on households; the incidence of the excise tax on residential construction will be on households and on land and development. The issue then remains: what happens, after taxes, to the non-residential portion of a property-tax increase as compared to an excise tax on new development?

The initial impact of a tax on new commercial development will be to decrease the potential profits in developing such properties. If this causes some slowing in the rate of new commercial development, it will slow down the escalation in land prices. The decrease in developers' profits and land prices will cause the increase in commercial rents (or capital investment, in the case of firms which own their own offices or stores) to be less than the amount of the tax. The impact on expansion, though very small, might have an effect on costs and on prices of services and commodities supplied by businesses in Montgomery County.

This excise tax would be treated as any other cost of doing business. Price is not necessarily adjusted automatically for every change in cost or demand; rather, pricing is part of broader corporate goals and policies. Many firms have price ranges with no exact price. A cost change may not necessitate an immediate price change -- an increase may be absorbed; a decrease, retained as profit.

The behavior of the business sector when it is faced with any increased cost of doing business -- including a property or excise tax increase -- will depend upon myriad factors: the type of property; general market conditions (is it a buyer's or seller's market?); the type of business; corporate pricing policies.

While any tax levied on new construction could ultimately be passed on totally to the new owner (i.e., consumer), much of it probably would not be.

Summary of the Differential Impact

A new development excise tax vis-a-vis an increase in property tax rates would make the County's homeowners and renters no worse off, even if a large portion of the tax were passed through in higher prices; but, since competition with existing facilities inhibits fully passing on costs, a lower burden would likely be imposed by the levy of a development excise tax than would a property tax increase. Additionally, new properties would bear a higher portion of the total receipts than of a property tax increase.

For new developments, some of the burden of the new tax may be paid by the State and Federal governments, while the balance will be distributed in varying proportions to shareholders through diminished profits, to employees through reduced compensation or working conditions, to consumers (some, but not all, of whom are County residents) by higher prices, and to owners of land held for development.

M72/59-60

MEMORANDUM

TO: County Council

FROM: MF Michael Faden, Senior Legislative Attorney

SUBJECT: Legal Validity of Excise Tax on Construction

DATE: April 26, 1990

We have reviewed the legal issues raised by Bill 34-90 and have prepared this memo to summarize our conclusions. We conclude that the County Council has the authority to enact an excise tax on construction as proposed in Bill 34-90, and that this tax is likely to survive constitutional challenges.

Legal Background

The basic statutory authority for the County to levy taxes, other than property taxes, is found in Montgomery County Code §52-17 (attached). §52-17 is a local public law enacted by the General Assembly in 1963. §52-17(a) gives the County, with certain exceptions specified in §52-17(b), "the power to tax to the same extent as the state has or could exercise such power within the limits of the County as part of its general taxing power;..."

Under §52-17(b), the County cannot adopt any tax that political subdivisions are prohibited from enacting under state law. This primarily means a sales tax, which counties generally cannot enact under Ann. Code Tax-General §11-102(b)(1). §52-17(b) also stops the County from enacting any income tax; tax on gasoline, motor vehicles generally, vehicle registration or titling; or gross receipts tax, among other more specialized taxes.

(The recent Eastern Diversified Properties case [No. 97, September Term 1989, decided March 7, 1990], in which the Court of Appeals struck down the County's impact fee law as an unauthorized tax, did not involve §52-17 and, in our view, does not undercut the County's authority under that law to enact this tax.)

The County also cannot adopt a narrowly-focused property tax. State law does not authorize them. The state Constitution (Art. 15 of the Maryland Declaration of Rights) has long been construed as requiring that all property taxes must be uniform in their application within the particular taxing district and prohibiting different taxes or rates for similar kinds of land. However, the uniformity principle does not apply to excise taxes. Weaver v. Prince Georges County, 281 Md. 349, 379 A2d 399 at 402 (1977), and cases cited therein.

In judging the validity of a tax, the Maryland courts focus on the kind of tax it is — whether the tax is a property tax, an excise tax (a catchall term for almost all taxes that are not based on the value of property), or a license fee or other regulatory measure. These are not always easy distinctions to make. The Maryland courts will give the "legislative label" put on the tax "considerable" weight, but it is not conclusive; the courts look mainly to the operation of the tax "rather than ... any particular descriptive language which may have been applied to it". Herman v. Mayor and City Council of Baltimore, 189 Md 191 at 198, 55 A2d 491 at 495 (1947).

A review of the leading Maryland cases shows that certain factors differentiate an excise tax from a property tax. The major factors are:

1. **What is the tax assessed on?** If it is ownership of the property, it is a property tax. If it is on a use of the property, or more specifically, if the tax is levied on only one of the "incidents of ownership", it is generally considered an excise tax. In the leading case, the Court of Appeals in Weaver v. Prince Georges County distinguished an excise tax involving real property from a property tax per se:

> ...the modern conception of an excise tax includes any tax not directly levied on the ownership of property as such. A tax on the use and enjoyment of a privilege appurtenant to property is, under this view, an excise, despite its close connection with the underlying property. 379 A2d at 406.

In Weaver, the Court upheld, as an excise tax, a 4% tax on rent paid for occupancy of multifamily residential units. In Herman v. Mayor and City Council the Court of Appeals upheld as an excise tax a Baltimore City tax of 50 cents per gallon on alcoholic beverages in the hands of retail dealers. The Court found the tax to be an excise tax "on the privilege of doing an alcoholic beverage business", rather than a property tax on the beverages. The Court held that it is not, in the legal sense, double taxation to apply an excise tax to property on which a property tax is also paid. Herman, 55 A2d at 496.

2. **Who pays the tax?** If the owner of the land pays it, it is more likely to be a property tax. If the operator of a business pays it, it is probably an excise tax.

3. **How is the tax measured?** If it "is computed upon a valuation of the property and is assessed by assessors, ... it is a property tax". Weaver, 379 A2d at 404, citing Montgomery County v. Maryland Soft Drink Association. If the rate is set in the legislation and is measured by the extent to which a privilege is exercised, it is an excise tax. This is true even if the unit of measurement is a unit of property. American National Building & Loan Ass'n v. Mayor and City Council of Baltimore, 245 Md 23 at 35, 224 A2d 883 (1965).

4. **When is the tax payable?** If a tax is payable at a specified date each year, it is more likely to be a property tax. If it is paid in connection with a transaction, it is probably an excise tax.

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5. **How is the tax enforced?** If a lien is automatically placed on the property when the tax is not paid, it is probably a property tax.

Care must also be taken to distinguish an excise tax from a sales tax, since the County can enact the former but not the latter. The major points of difference are first, that a sales tax is triggered by a taxable event, a sale, rather than (as with the County beverage container tax, Code §52-16B) merely a distributor supplying the property to a dealer; second, a sales tax is measured by the price paid for the property, rather than (as with the beverage container tax) the number of items and their capacity. Montgomery County v. Maryland Soft Drink Association, 281 Md. 116, 377 A2d 486 at 491-2 (1977).

Finally, the law separates license fees, which are regulatory exactions based on the police power, from excise taxes, which are primarily intended to raise revenue. If the statute requires compliance with prescribed conditions in addition to the payment of money, it is a license fee; but if its sole or primary purpose is to raise revenue, and no other conditions attach to the payment, it is a revenue measure. Maryland Theatrical Corp. v. Brennan, 180 Md. 377 at 381, 24 A2d 911 (1942); see American National Building & Loan Ass'n v. Mayor and City Council of Baltimore, 245 Md 23 at 33-34, 224 A2d 883 (1965). This distinction is important because a regulatory measure must have a rational relationship to the goals it is intended to achieve, while revenue-raising laws are not held to this standard even though they may have a secondary regulatory effect. Excise taxes, in particular, are given wide leeway, and the Maryland courts are very reluctant, compared to those of some other states, to second-guess legislative classifications in this area. See Reinhardt v. Anne Arundel County, 31 Md App 355, 356 A2d 917 at 922 (1976).

Application to Bill 34-90

Applying all these factors to Bill 34-90, a reviewing court is very likely to conclude that the proposed tax on construction is, legally as well as in name, an excise tax that the County has full power to enact.

In Montgomery County v. Maryland Soft Drink Association, the Court of Appeals held that §52-17 authorized the County to enact an excise tax on certain beverage containers. Thus, if the tax proposed in Bill 34-90 is an excise tax and not a property tax, §52-17 authorizes the County to enact it.

An analysis of the previously-mentioned factors that distinguish excise taxes from property taxes indicates that the tax proposed in Bill 34-90 is clearly defensible as an excise tax. (When a similar excise tax was proposed in Bills 11/12-86, the then-County Executive strongly opposed the tax as a matter of policy but never questioned the Council's authority to enact it.)

1. **Subject matter of the tax**. The tax proposed in Bill 34-90 is not assessed on ownership of property. It is assessed on the act of construction on the property. As two experts said in a recent book:

> It is clear ... that an excise tax on new construction must be imposed on the person undertaking such new construction rather than on the land itself or on the process of subdivision or issuance of a building permit.

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An excise tax is a tax on an individual's economic activity. The tax may be collected at building permit issuance if that is simply a convenient point to ascertain the amount of the tax to be imposed and is not construed as a tax on the building permit itself. Strauss and Leitner, Excise Taxes: Impact Fee Alternative, in Development Impact Fees (Nelson, ed., Planners Press, Am. Planning Ass'n, 1988), p. 164.

Here the issuance of the building permit is not, on the face of the law, the event that triggers the tax; rather, it is the fact of construction. As Strauss and Leitner suggest, the building permit issuance or application (depending on whether the permit is issued by the County or a municipality) is only a convenient point at which to assess the tax and assure its payment.

The Court of Appeals in Weaver cited with approval cases from New York, Pennsylvania and Florida that sustained excise taxes on the occupancy and rental of commercial property. 379 A2d at 404-5. In another relevant case, the Colorado Supreme Court upheld a municipal "Service Expansion Fee" imposed on persons who obtained building permits for new construction or substantial rehabilitation. The Fee was based on the type of development and its square footage. Cherry Hill Farm v. City of Cherry Hills, 670 P2d 779 (1983). Although the lower court had struck down the Fee as a general ad valorem property tax, the state Supreme Court held that because it was levied on the use of property without regard to its value, and because it was on the privilege of improving the property by construction and not the property itself, the Fee passed muster as an excise tax. The court distinguished a 1978 Colorado case that struck down, as a non-uniform property tax, another municipal service expansion fee that was based on the value of the property under construction.

2. **Who pays the tax**. Under Bill 34-90, the tax is paid by the person who intends to build or add to the building. Thus, the tax is on the person who undertakes a business activity. That person is not necessarily the owner of the property.

3. **Measurement of the tax**. Under Bill 34-90, the tax is measured by the size (square footage) of the building or addition. It is not measured by either the cost of construction (as with a sales tax) or the value of the property during or after construction.

4. **When payable**. This tax is payable only once, when the applicant for a building permit proposes to build or add to a building. It is not assessed or payable annually.

5. **Enforcement**. Under proposed §52-51, the tax is enforceable by criminal penalties, civil penalties and assessment of interest on unpaid taxes. In addition, §52-50(e) applies §52-18D to this tax. §52-18D is a lien provision used for a number of County excise taxes. Because this lien applies only to excise taxes, a court would be less likely to treat it as one of "the attributes traditionally associated with a conventional property tax" (Weaver, 379 A2d at 407).

Pulling all these factors together and keeping in mind the Maryland courts' relatively broad definition of excise taxes, we conclude that this tax is authorized by the local public law codified in §52-17 and is likely to be upheld as an excise tax and not struck down as a disguised property tax.

Sec. 52-17. Additional taxing powers; prohibited taxes.

(a) *Generally.* The county council is hereby empowered and authorized to have and exercise, within the limits of the county, in addition to any and all taxing powers heretofore granted by the general assembly, the power to tax to the same extent as the state has or could exercise such power within the limits of the county as a part of its general taxing power; and to provide by resolution for the imposition, assessment, levy and collection of any tax or taxes authorized by this section; and from time to time to grant exemptions and to modify or repeal existing or future exemptions.

(b) *Exceptions.* Provided, that the council shall not have the power to impose any tax upon any alcoholic beverages, intangible personal property or upon the subject matter of Annotated Code of Maryland, 1957, sections 135 to 157 of article 56 (gasoline tax); sections 3-601.1, 3-801 to 3-824, 11-706, 14-112 of article 66½ (motor vehicle registration); section 3-831 of article 66½ (titling tax); sections 181 to 190 of article 56 and section 273 of article 81 (motor vehicle taxation); section 9(32) of article 81 (class A and class D motor vehicles); sections 279 to 323 of article 81 (tax on incomes); article 78B (horseracing and pari-mutuel betting); sections 194 and 195 of article 81 (bonus tax); sections 197 to 201 of article 81 (tax on franchise to a corporation); sections 129 and 130 of article 23 (recording corporate papers); section 128 of article 81 (deposits of savings banks); sections 135 to 143 of article 81 (insurance premiums); sections 149 to 193 of article 81 (inheritances); article 62A (estate tax); or section 144 of article 81 (tax on commissions of executors and administrators); or sections 431 to 464 of article 81 (state tobacco tax act) or sections 12-A and 12-B of article 81 (sales tax and gross receipt tax on advertising, etc.) to the extent applicable; or any other tax prohibited to a political subdivision of this state by any applicable statewide law; nothing in this section shall be construed to authorize the county to impose a tax upon the gross receipts of any person in the county; provided, however, that the county in taxing the receipts, from motor vehicle operations, may only tax receipts from operations of motor vehicles having a permit from the Public Service Commission of Maryland authorizing both the taking on and discharging of passengers at more than one (1) point within the county and/or the transportation of passengers between two (2) or more points within the county.

(c) *Advertisement required.* On or after June 1, 1963, no tax shall be levied or imposed by the county pursuant to any of the provisions of this section unless the levy or imposition of the tax is advertised for three (3) consecutive weeks in two (2) newspapers having a general circulation in the county. After such advertising a public hearing shall be held concerning the levy and imposition of such tax. The provisions of this section shall not apply to any tax levied and imposed prior to June 1, 1963. (Mont. Co. Code 1965, § 2-129; 1963, ch. 808, § 1.)

M E M O R A N D U M

March 29, 1990

TO: Robert Kendal, Director, Office of Management and Budget
Andrew Mansinne, Director, Office of Legislative Oversight

FROM: MF Michael Faden, Senior Legislative Attorney

SUBJECT: Bill 34-90, Excise Tax - Construction

The attached bill was introduced by the Council on March 13, 1990, and is scheduled for public hearing on April 17, 1990.

Please provide the Council with your respective fiscal and economic impact analyses and recommended evaluation procedure. I would appreciate receiving your responses as soon as possible.

Attachment

April 5, 1990

TO: Michael Faden, Senior Legislative Attorney

FROM: Andrew Mansinne, Jr., Director, Office of Legislative Oversight Andrew Mansinne

SUBJECT: Evaluation on Bill 34-90, Excise Tax - Construction

Evaluation. Recommend that an evaluation of the Excise Tax - Construction be conducted during the year before the proposed June 30, 1996, sunset date of the tax. The evaluation can be conducted by either OLO or the Executive branch (OMB).

PUBLIC HEARING
April 2 & 4, 1991

91 APR 1 P2:31

Montgomery County Government

ROCKVILLE, MARYLAND 20850

Neal Potter
County Executive
(301) 217-2500
TTY 217-6505

24-90

M E M O R A N D U M

April 1, 1991

002530

TO: Isiah Leggett, President, Montgomery County Council

FROM: Neal Potter, County Executive

SUBJECT: Construction Excise Tax

I recommend that the Council approve a construction excise tax with the features detailed below. The Council has introduced for public hearing on April 2, 1991, Bill 34-90, which I supported last year. In order to allow for Council action after that hearing, I am submitting my proposal as an amendment to Bill 34-90 in the form of a replacement. My proposal is attached. The public hearing notice was sufficiently broad in scope to include my recommendations.

Description of Features

The features of my recommended construction excise tax are as follows:

1. Effective date of April 1, 1992.

2. Tax per square foot (sf) of gross floor area, varied by building type: residential - $3.75; places of worship and schools - $1.00; warehouse and manufacturing - $3.00; all other nonresidential - $5.00.

3. Exemption for the first 800 sf of any new building and the first 400 sf of any addition. In multifamily structures, the first 800 sf of each dwelling is exempted.

4. Exemptions for government buildings.

5. Exemption for housing projects developed under a government or nonprofit program that assures price control, e.g., MPDU.

6. Credit given for payment of existing development impact tax in Germantown and Eastern County.

7. Rates to increase with CPI. Rates may also be adjusted by Council resolution, after public hearing.

8. Tax payable at building permit approval or building permit renewal/reapproval. If property is not yet subdivided, then collect 30 percent of estimated tax at approval of preliminary subdivision plan and remainder at building permit approval.

9. Revenue to be used for CIP debt avoidance, except that the Executive may recommend using up to one-third of anticipated budget year revenue for CIP debt service.

10. Development districts may be created where circumstances warrant, without affecting the obligation to pay this tax.

Revenue Estimates

The official Planning Department forecast for the next five years shows an average of about 6,000 DU per year. That much housing construction would generate an average of about $21.8 million per year in tax revenue. The Planning Department provided on February 7, 1991, an updated forecast for the next four years which has as its low average 4,500 DU per year and its intermediate average 6,750 DU per year. For future average annual revenue, 6,000 DU is used.

If employment growth were to match the Growth Policy goal of 1.5 jobs per DU, then 9,000 jobs per year @ 250 sf per job would generate about 2,250,000 sf in nonresidential construction and $9.9 million per year in tax revenue. Last spring, the M-NCPPC Planning Department forecasted an annual average of 4.0 million sf of nonresidential construction. Recently, the Department prepared a revised forecast for the next four years with an average of 2.1 to 2.45 million sf per year. For future average annual revenue, 2,250,000 sf is used.

The average annual total revenue would be $31.7 million. Net revenue would be reduced by the credit given for the existing Germantown and Eastern County impact taxes, which recently averaged over $2 million per year.

Of course, because of the recession, revenue for the first 12 months of collection, starting in FY 92, would be a small fraction of those amounts. Given the current office space vacancies and the absence of financing for new construction, we expect only a nominal amount, say 200,000 sf, of nonresidential construction permits in FY 92. Housing construction may fall to its lowest level in recent decades, in the range of 1,500 DU. With these assumptions, revenue would be $6.3 million. Subtract, say, $500,000 for credits for Germantown and Eastern County impact taxes, and first year revenues would be about $5.8 million. Since I propose that the tax be effective April 1, 1992, there would be only three months of revenue in FY 92, or about $1.4 million.

Cost of Collection/Administration

Given established procedures for collecting payments with building permits and experience with the existing development impact taxes in Germantown and Eastern County, collection of the construction excise tax at building permit approval should be straightforward. A complexity is introduced with collection of part of the tax at approval of the preliminary subdivision plan. Guidelines can be created readily for estimating the amount of tax ultimately payable and procedures can be established for having the Planning Department collect the amount due at subdivision and remit it to the County Finance Department. A system might be needed also to allow verification of claims at building permit for partial payments made at subdivision. However, principal responsibility for supporting a claim for credit at building permit would rest with the applicant for the building permit. The bill provides that subdividers who sell lots to builders must incorporate into their sales contracts an agreement about the credit for any partial tax payment made at subdivision.

Another issue is collection within municipalities. Collection within municipalities without a County building permit could be complex. Ideally, those municipalities would cooperate with the County and require evidence that the County development tax had been paid before the municipal building permit would be issued. For the convenience of builders, municipalities might agree to collect the County tax and remit it to the County. Since the County collects municipal property taxes without charge, the County can reasonably ask for cooperation on municipal collection of this tax. If cooperation could not be established, then the County Finance Department would have to get copies of municipal building permits, compare with Finance Department records of construction excise taxes paid, identify noncomplying builders, figure the tax due, and send bills to the builders. Under that scenario, achieving full compliance would be much more difficult.

Assuming that municipalities would cooperate, we estimate that annual costs of administration would probably be less than $100,000 for additional clerical time, accounting, management information reporting, and supervision.

Attached Tables

Attached as pages eight and nine are two tables which display the recommended tax rates, the effective tax on typical buildings, and the total estimated revenue. The tables differ only in the estimated quantity of construction. Page eight shows the estimated five-year annual average of construction and revenue. Page nine shows the estimate for the first calendar year of operation, starting in FY 92.

Effective Date

Since the proposed tax would be a significant additional cost of development, I recommend an effective date of April 1, 1992. This one-year lead time from today will allow projects negotiated in the absence of this tax to proceed. Although the development community has had ample notice of my intent to support a tax on new construction, developers have not seen this specific proposal. Given the currently fragile real estate economy, adding an unanticipated tax could forestall some projects that might otherwise move ahead in the coming year and provide needed employment opportunities. However, it is essential to enact the tax promptly and make very clear the County's intention that the next significant growth period will pay more of its own way than has been the case in the past.

Tax Level

The tax rate of $3.75 per sf, with the 800 sf exemption, results in a tax of $6,000 for the average-sized detached house. The $6,000 figure was selected as a benchmark because it generates significant revenue while keeping up-front charges to developers below the burdens developers bear in other jurisdictions in this region, excepting Prince George's. See the table on up-front costs for water and sewer, page ten. The main point of that table is that developers in the Washington Suburban Sanitary District, which is most of Montgomery and Prince George's Counties, pay almost no up-front costs for water and sewer, in contrast to the $7,000 to $10,000 per lot costs to developers in other jurisdictions.

It must also be noted that property buyers pay in special assessments in the Sanitary District most of the costs avoided by the developers. For example, the buyer of a new house today with a 90-foot frontage would probably pay WSSC about $700 per year in special assessments on the property tax bill for 23 years.

Another qualification to the conclusion on developers' costs in Montgomery County is the cost of off-site transportation improvements sometimes required to meet adequate public facilities (APF) tests and thus allow a project to proceed on the developer's preferred schedule.

Data on impact fees in other jurisdictions in the area has been collected. Impact fees for detached houses in other Maryland counties are: Anne Arundel, $2,629; Calvert, $3,000; Carroll, $3,500; Charles, $3,500; and St Mary's, $2,000. The Town of Poolesville levies an impact fee for recreation and other public facilities of $2,327 per house, which is in addition to water and sewer costs of about $10,000. In Anne Arundel County, developers pay a county road/school impact fee of $2,629, plus water and sewer costs of $8,870 (1988 level). In Fairfax, developers pay over $10,000 for water and sewer plus whatever the county can get in proffers. The Germantown and Eastern County impact tax rates are shown on pages 11 and 12.

Despite some gaps in our knowledge of comparative costs of development among jurisdictions, a tax of $6,000 on the typical detached house seems reasonable. The tax rates proposed for nonresidential development produce effective tax rates of about five percent of construction cost.

Credit for Off-Site Improvements

Credit against the Countywide tax would be given for any payment of the existing Germantown and Eastern County impact taxes.

The existing development impact taxes allow credit for developer construction of elements of the particular transportation projects listed in the County Code in Section 52-57. The rationale for the credit is that those projects are the cost basis for the tax and that therefore it would be unfair to both collect the tax and require the developer to construct part of the project.

No similar credit is proposed in the Countywide construction excise tax. This tax is to be used for general support of the CIP and is not tied to particular projects. Construction of off-site improvements is required by the Planning Board as a condition of subdivision approval when necessary to meet APF requirements; a developer who chooses to accept those requirements does get approval to build.

Although no general credit for off-site improvements is proposed, I recognize that this issue warrants further consideration in the future, once the Countywide tax is in place. As we gain some experience with the new tax, there should be a review with the Planning Board of the extent and cost of off-site requirements.

Partial Payment at Subdivision

There are two reasons for collecting 30 percent of the estimated tax at subdivision approval. The first is the County's need for some revenue earlier in the development process in order to help fund road projects that will be needed for the additional traffic associated with those developments. The second is that the tax will discourage premature applications for subdivision that preempt APF capacity from subsequent developers who are ready to build.

Use of Revenue

The purpose of this tax is to provide general support to the capital improvements program. Normally, the revenue would be used to avoid issuing bonds. However, the Executive could recommend that up to one-third of the anticipated revenue for any budget year could be used for debt service on bonds previously issued.

Development Districts

A development district is a special taxing district that would be created by specific legislation, just as other special taxing districts have been in the past. As currently envisioned, a development district would contain a substantial percentage of developable land. Within a development district, special taxes would be levied to pay for transportation capital projects necessary to serve the area well and to lift any APF moratorium. Special taxes could also be used to pay for higher levels of operating services.

Areas under consideration for establishment of development districts are Shady Grove and Germantown Town Center. Taxes under consideration include a development excise tax, a property tax for capital improvements (which would be exempt from the Question F limit), and different forms of a parking tax.

Participation in a development district would not exempt a developer from paying the Countywide construction excise tax, but would assure APF approval for a staged buildout.

IMPACTS

A useful way to illuminate the impact of the proposed tax is to compare it to alternative ways of raising the same $30 million in average annual revenue. The principal alternative to the construction excise tax is the general property tax.

The County would receive $30 million from either a 12.8-cent property tax rate increase (FY 91 base) or the proposed excise tax on new development. The initial incidence of a property tax rate increase would be 67 percent ($20.1 million) on existing residential property and 33 percent ($9.9 million) on existing nonresidential real and personal property. For the excise tax, 100 percent of the initial incidence would be on developers of new properties.

Since both households and businesses can deduct property taxes from their State and Federal income taxes, these treasuries will pay a portion of the property tax increase, at applicable marginal rates, for those who itemize deductions. The development excise tax would be a business expense for developers and therefore should also be deductible for State and Federal income tax purposes. Thus, some of the excise tax burden would also be transferred to those levels of government.

With a property tax increase, owner-occupants, both residential and commercial, have no way, other than income tax deductions as noted previously, to pass on the cost to other parties. Owners of rental properties, both residential and commercial, will try to pass on their cost increases to tenants, but will be limited in varying degrees by market conditions.

Although a property tax rate increase would apply to existing properties (and to future improvements when built), a construction excise tax would apply only to new improvements. The excise tax could be avoided by not building.

In economic theory, the rational developer/entrepreneur will charge what the market will bear, regardless of costs of development, including excise taxes. From this theoretical perspective, an increase in development cost, such as the excise tax, would have to be absorbed by the developer in reduced profit, since the sales price would have been already set as high as it could be. In the short run, if the developer already owned the land, he would either build at less profit or decide not to build. If the developer did not own the land, he would try to negotiate a lower land price and the cost of the tax would be split between the land owner through a lower land sale price and the developer through a lower development profit. Over a period of time, land prices would have to adjust to the point where a developer could make a reasonable profit and still sell at a price acceptable to buyers and renters of residential and commercial buildings. A land owner who insisted on a higher price than this optimum would not find a buyer.

This rational entrepreneur theory assumes that prices to the consumer are already at the maximum level the market will bear and that therefore there is little opportunity to make the consumer pay more. However, in the real world, developers are often not sure what the maximum prices are that the market will bear. If current costs allow a reasonable and customary profit to be earned, the developer may not try to test the market by raising prices. If costs should be increased by a construction excise tax, then the developer would probably be more inclined to try to raise prices to protect current profit margins. Competition with existing buildings and with other jurisdictions would place some constraints on that effort. In some cases, the market would accept higher prices and some of the excise tax would be passed through to consumers.

In the real world as well as in theory, land prices do respond to what developers can afford and are willing to pay. In the current real estate recession, there have been articles in the real estate press about falling land prices. When the consumer resists paying higher prices to the developer and the developer has constrained his development costs and his profit as much as he is able, he will be limited in what he can afford to pay for land. Some builders would argue that the current and foreseeable supply of land eligible for subdivision in Montgomery County has been so constrained by road capacity/APF problems and sewer service availability that owners of developable land enjoy a sellers' market and cannot be made to lower their prices. However, the weight of argument suggests that, in the long run, owners of vacant land will probably have to absorb a significant part of the cost of the excise tax.

The existence of a large base of existing buildings for sale and for rent in Montgomery County and the region will constrain the ability of developers of new projects to raise prices, and competition from new projects elsewhere in the region will limit price increases in Montgomery. At the same time, higher costs for new construction will tend to allow existing property to be sold or rented for higher prices, thus affecting all consumers.

In conclusion, market conditions within Montgomery County and in the region will determine the sharing of the cost of the construction excise tax among consumer, developer, and land owner. It is also reasonable to expect that the pace of new development would be slowed slightly below what would otherwise occur since the cost of the tax will cause some potential projects to cross a narrow line into infeasibility, at least temporarily.

In comparison with a property tax, the construction excise tax would have little or no impact on existing homeowners who do not intend to buy a different house. In the short run, developers and buyers of new construction would be affected more by the excise tax than the property tax. In the long run, owners of vacant land would also be more affected by the construction excise tax than the property tax.

MP/sa

Attachment: Amendment to Bill 34-90

UP-FRONT COSTS BORNE BY DEVELOPERS
FOR WATER AND SEWER

Charges represent developer costs for a single-family dwelling on a lot with 90 foot frontage.

	WSSD MONTGOMERY	WSSD P.G.	ANNE ARUNDEL	HOWARD	ROCKVILLE	FREDERICK	FAIRFAX	ARLINGTON	ALEXANDRIA	LOUDOUN
WATER & SEWER CONSTRUCTION										
Water Permit/Inspect	$35	$35	$25	$10	$75					$40
Sewer Permit/Inspect	$35	$35	$25	$15	$75					$40
Plumbing Permit	$100	$100								
Water/Sewer Main Extensions	a	a	a	a	a	a	a	a	a	a
Water Lateral Lines			$2,070 b	$2,070 b	$2,070 b	$2,070 b	$2,070 b	$2,070 b	$2,070 b	$2,070 b
Sewer Lateral Lines			$3,420 b	$3,420 b	$3,420 b	$3,420 b	$3,420 b	$3,420 b	$3,420 b	$3,420 b
Water House Connections *			$455	$55	$555	$600	$750	$1,500	$400	$466
Sewer House Connections			$775		$755	$775	$775	$775	$775	$775
Water - Major Facilities			$1,200 c	$600	$913	$1,500	$750	$216	$678	$1,868
Sewer - Major Facilities			$900 c	$600 c	$913	$1,500	$2,500	$488	$1,080	$1,537
TOTAL WATER & SEWER	$170	$170	$8,870	$6,770	$8,776	$9,865	$10,265	$8,469	$8,423	$10,216

FOOTNOTES:

a. In all jurisdictions except WSSD (see explanatory notes for WSSD), developers construct water and sewer main extensions at their own expense. The cost will vary depending on how far a main must be extended to reach the subdivision.

b. In all jurisdictions except Montgomery and Prince George's, developers construct and pay for the water and sewer lateral lines within their subdivisions. The cost is borne by the developer but is not a payment to a public agency. Therefore, an estimate must be made for this chart. The figures used are the average costs for such construction by WSSC for the year ended 9/30/87, $23 per front-foot for water and $38 for sewer, multiplied by 90 front-feet.

c. An additional charge is paid by some developers. See explanation for that jurisdiction.

* Includes water meters where applicable. See explanatory notes.

OMB 10-11-88

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Exhibit 1

CURRENT AND PROPOSED TAX SCHEDULES FOR THE GERMANTOWN IMPACT TAX DISTRICT

Land Use Type	Current Rate	Proposed Rate
Single-family residential (per dwelling unit)	$1,489	$1,814
Multi-family residential (per dwelling unit)	$992	$1,209
Office (per 1,000 sq. ft. gross floor area)	$3,355	$4,090
Industrial (per 1,000 sq. ft. GFA)	$1,459	$1,778
Retail (per 1,000 sq. ft. GFA)	$3,035	$3,698
Places of Worship (per 1,000 sq. ft. GFA)	$175	$213
Private Elementary and Secondary Schools (per 1,000 sq. ft. GFA)	$293	$356
Other Non-Residential (per 1,000 sq. ft. GFA)	$3,355	$4,090

Exhibit 2

CURRENT AND PROPOSED TAX SCHEDULES FOR THE EASTERN MONTGOMERY COUNTY IMPACT TAX DISTRICT

Land Use Type	Current Rate	Proposed Rate
Single-family residential (per dwelling unit)	$1,855	$956
Multi-family residential (per dwelling unit)	$1,237	$637
Office (per 1,000 sq. ft. gross floor area)	$4,182	$2,156
Industrial (per 1,000 sq. ft. GFA)	$1,819	$937
Retail (per 1,000 sq. ft. GFA)	$3,783	$1,949
Places of Worship (per 1,000 sq. ft. GFA)	$218	$113
Private Elementary and Secondary Schools (per 1,000 sq. ft. GFA)	$365	$188
Other Non-Residential (per 1,000 sq. ft. GFA)	$4,182	$2,156

MONTGOMERY COUNTY COUNCIL
ROCKVILLE, MARYLAND

BRUCE ADAMS

April 9, 1991

MEMORANDUM

TO: Marilyn Praisner

FROM: Bruce Adams

SUBJECT: Bill 34-90, Excise Tax - Construction

As your committee reviews Bill 34-90, Excise Tax - Construction, I would ask that you focus on what I believe are two fundamental points:

First, the bill should be amended to reflect the reality of the economy by delaying the effective date and phasing in the excise tax. Our building industry has quite obviously not recovered and our legislation should take that reality into account.

Second, we should pass this bill now so we do not relive the mistake previous Councils made in the 1980s of not having a development tax in place during a building boom. For years and years, the industry has argued that now is not the time to adopt this tax. There never will be a "right time" in the view of the industry. We should act now to be sure the tax is in place when the economy recovers, and we should phase it in so that builders can plan for it well in advance.

Phasing-In the Tax

The bill was introduced in March of 1990 and is applicable to any construction for which an application for a building permit is filed on or after September 1, 1990. We included a Sunset provision terminating the tax after June 30, 1996 and requiring an Office of Legislative Oversight evaluation by October 31, 1995.

I propose that the tax be phased-in as follows (the dates refer to time of building permit issuance):

January 1, 1992	$1 per square foot
July 1, 1992	$2 per square foot
January 1, 1993	$3 per square foot.

I prefer this proposal to the County Executive's suggestion for full implementation of the tax on April 1, 1992. Some construction is going forward and we should begin soon to tax it even if only modestly. By phasing in the tax, we will minimize the competitive unfairness in the marketplace of one project applying in March of 1992 with no tax and the project next door applying in April and being hit with the full tax. It is my hope that by phasing in the tax in three parts, we might encourage bankers and builders to move somewhat faster towards construction than they might otherwise. This might help speed the recovery.

I have not had time to explore fully the proposal by West Farm to collect half the tax at building permit and the other half at occupancy permit. It does have the advantage to the developers of not having to pay until they have an income stream. It is worthy of careful consideration. The disadvantage is that infrastructure that is dependent on the tax will lag.

I would retain the Sunset provision but change the date to June 30, 1997 and the OLO evaluation date to October 31, 1996.

Application of the Tax

Based on the testimony we heard at the public hearing last week, I would maintain a uniform fee for all building types, and I would not change the bill's exemption for certain nonprofits as the County Executive has proposed.

I favor the 1,200 square foot exemption because of my concern that this tax not have an undue negative impact on affordable housing. I agree with the County Executive that the bill should be made clear that the exemption applies to each unit of multifamily housing.

The bill proposes a credit for impact taxes. The 1986 impact fee law has produced too little too late. Given the current disposition of the banking community, I expect that most projects that need major infrastructure financing will require development districts that allow developers and landowners to pay over time rather than up front. I suggest that the issue of credit for development district contributions be addressed when we take up development district legislation.

Amount of the Tax

I am proposing an ultimate $3 tax rather than the $3.25 in the bill or the higher taxes proposed by the County Executive because I believe it is essential that we request authority from the General Assembly to allow WSSC to charge developers the cost of sewer and water expansions. I believe the likely 23% WSSC rate increase in FY 93 is intolerable. If we do not obtain this authority, I would support a higher development tax.

Use of the Tax Revenue

My work as co-chair of the Task Force on Growth & Transportation at the Council of Governments has confirmed my belief during my first term on the Council that our county and our region are facing a crisis in infrastructure financing. Traditional funding sources are not sufficient to finance needed roads, schools. and other public facilities. Our county and state transportation budgets have been decimated. The state is not providing nearly the amount we need for school construction. And the national administration continues in full retreat from its responsibilities in transportation and housing.

In the past, we have expected our residents to pay for the roads, schools, libraries, and other public facilities for those who moved here after they did. This was fair because someone had paid for the infrastructure they used. Unfortunately, the excessively rapid pace of growth in the middle and late 1980s combined with the extraordinary escalation of infrastructure costs has taken these costs beyond what existing property taxpayers alone can be asked to finance. Unless we are to strangle all new growth in our AGP and APFO moratoria, we simply must have a significant contribution from the developers, landowners, and new residents and businesses that will benefit from new infrastructure. These growth moratoria are a far greater threat to affordable housing than the development tax. The development excise tax proposed in Bill 34-90 is the first step. Development district legislation should follow shortly.

I favor allocating the first $5 million raised by the tax each year to the Montgomery Housing Initiative. Every year we have battled the Executive for these funds. This year, the Executive has proposed that we add no new money to the fund. The development tax would be a far more reliable source of funds than relying on annual budget battles with the Executive. As the Housing Opportunities Commission has pointed out, we very much need these funds.

I would allocate additional funds each year from the tax to the CIP. I agree with those who say that added growth places a large burden on our operating budget, but I believe it is more appropriate to use the money to build the infrastructure that new growth requires. We are failing badly at this time in building needed infrastructure.

For this year, because of the delayed effective date, the phase-in of the tax, and the state of the economy, I believe we should not allocate any of the potential revenue to the CIP other than to the Housing Initiative. Whatever additional taxes are collected can be allocated in the FY 93-98 CIP.

Thank you for your consideration of my thoughts. Obviously, much has changed since we introduced this bill last year and amendments are needed. I look forward to working with you on this important legislation.

BA:tb:33/66-68

Copy: County Executive
County Council
Planning Board

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COUNCIL

91 APR 29 P1:04

34-90

NRN
cc
MF

April 23, 1991

003622

William E. Hanna, Council Member
Montgomery County Council
100 Maryland Avenue
Rockville, Maryland 20850

Re: Federal Tax Treatment of Proposed <u>Construction Excise Tax</u>

Dear Council Member Hanna:

I am writing to share with you our interpretation of the likely Federal tax treatment of the proposed construction excise tax. Although we have not had an opportunity to review the version of the legislation most recently approved by the Management and Fiscal Policy Committee, we understand that the proposed construction excise tax would be imposed on builders in Montgomery County at the time of the issuance of building and/or occupancy permits.

My colleague, Dick Ruprecht of our Tax Department, has confirmed that the payment of such a tax by an owner/user of the property would not result in an offsetting deductible expense, but rather under Section 263A of the Internal Revenue Code would have to be capitalized and depreciated over the depreciable life of the property. Thus, at most, the owner user would be entitled to a current deduction equal to a small fraction of the actual taxes paid.

A similarly onerous treatment is applicable to a builder who constructs property for resale as inventory. Again, under Code Section 263A, most such builders would not be allowed an immediate deduction but rather would have to include the construction excise tax expense in inventory costs for the property, with a resulting delay in the deduction until the property is sold.

The above tax treatment is in marked contrast with that applicable to local property taxes which are fully deductible when paid or incurred by either business or nonbusiness property owners.

Mr. Ruprecht and I are available to discuss further with you the impact of the proposed construction excise tax and the particularly harsh Federal tax treatment that would result. Please feel free to call us at 986-1300 if we can be of further assistance.

Sincerely yours,

Harry

Harry W. Lerch

RMR:skc
cc: Isiah Leggett, President
tax/rmr\mcc.2
42391/3

Bechtel Investments, Inc.

Fifty Fremont Street, Suite 3700
San Francisco, California 94105

May 6, 1991

Michael Faden
Senior Legislative Attorney
Montgomery County Council
100 Maryland Avenue
Rockville, Maryland 20850

Re: Montgomery County Bill 34-90 Excise Tax - Construction

Dear Michael:

In conversations during the last month, we have been discussing the deductibility of a tax on new construction in Montgomery County (the "County") which would be levied through the statute enacted by County Bill 34-90. Below is a summary addressing the deductibility of state and local taxes, and a revised version of County Bill 34-90, which we would suggest as an alternative. This alternative should generate the same tax revenues for the County, from the same sources, but should also be deductible for federal income tax purposes; and would therefore be more equitable to taxpayers. This alternative is intended to addresses the tax deductibility issue only, and is not intended to address any other non-tax issues related to the Bill.

Deductibility of State and Local Taxes

A deduction is allowed for state and local taxes on income, property and profits where the primary purpose of the tax is to raise revenue. IRC § 164(a); Treas. Reg. § 1.164-1. A deduction may be claimed under section 164 regardless of whether the tax is incurred in an active trade or business. However, taxes paid or incurred in the acquisition of property are treated as part of the cost of such property. Id. Accordingly, such taxes cannot be currently deducted but must be capitalized into the tax basis of the property and are recovered through depreciation. Id.

State and local income taxes, and personal and real property taxes, are the only state and local taxes deductible as taxes under section 164. Further, some state payments designated as taxes or fees are not deductible as taxes under section 164. IRC § 164(c); Treas. Reg. § 1.164-1(g). However, state or local fees and taxes that are not deductible as a tax under section 164 may be deductible as a business expense under section 162, if such fees or taxes are paid or incurred in the conduct of the taxpayer's active trade or business or investment activity. IRC § 164(a); Treas. Reg. § 1.164-1(a).

As an alternative to the Bill as currently drafted, we would suggest that the County enact an annual tax that would be imposed on buildings or additions constructed after the effective date of the proposed statute ("newly constructed buildings") based on the leased or occupied square feet in the building or addition where the building is retained by the builder. Where the building is sold before the building has been leased or occupied, the tax would be based on the total square footage of the newly constructed building or addition. In the case where a newly constructed building is leased or occupied and then sold, the tax would continue to be paid by the purchaser. This fact is helpful in arguing that the tax is currently deductible.

Enclosed is a revised version of the proposed County Bill 34-90 which adopts this alternative. The tax rate proposed in the Bill is the same as in the original bill for newly constructed buildings or additions that are sold. In the case of leased or occupied buildings or additions, the tax rate is set at an annual amount that will generate the same amount of revenue over a ten year period. The tax is due within thirty days of the date on which the building is first leased or occupied and on January 1, of each calendar year thereafter for nine additional years. Under the revised version of the Bill, the statute sunsets in 2002.

The revised bill also has the same exemptions as the earlier version and the same collection procedures. Under the revised version of the Bill, a leased or occupied building, (such as an owner occupied building) is taxed only on the square footage that is actually leased or occupied in any given year.

In the case of a leased or occupied building, the tax imposed by the revised Bill should be currently deductible under section 164 as a tax on real property for the purpose of raising revenue for the general public welfare in the County. Even if the tax fails to be deductible under section 164, the tax should also be deductible under section 162 as an ordinary and necessary business expense, as the expense is reoccurring annually and clearly has a useful life of less than one year.

In the case of a newly constructed building or addition that is sold, the tax levied by the revised Bill would reduce the amount of gain from the sale that would be otherwise subject to tax. Where the building is sold at a loss, the tax would increase the tax loss from the sale.

The type of tax as provided for in the revised County Bill 34-90 is also more equitable to the taxpayer as the tax is due only when the newly constructed building or addition is leased, occupied (and accordingly used in the taxpayer's trade or business), or sold, and

Section 162 provides a deduction for ordinary and necessary expenses of a taxpayer in carrying on a trade or business. IRC § 162(a). An expenditure is not deductible under section 162 where the expenditure provides a benefit beyond the current tax year. Moreover, an expenditure that is a cost of acquiring a capital asset is properly characterized as a capital expenditure that must be added to the tax basis of the property acquired. Oriole Homes Corp. v. United States, 89-2 USTC ¶ 9433 (S.D. Fla. 1989); Lots, Inc. v. Commissioner, 49 T.C. 541 (1968).

For real property taxes to be currently deducted, such taxes must be levied against the real property interest, and the purpose of such taxes must be to raise revenue for the general public welfare. Treas. Reg § 1.164-3(b). A tax imposed on the rent paid by a tenant is not a tax under section 164 as it is not imposed on the real property interest. Rev. Rul. 75-346, 1975-1 C.B. 66. However, such tax is currently deductible under section 162 as an ordinary and necessary business expense, as the tax is recurring annually. Therefore, such tax does not provide a benefit beyond the current tax year, and is not expended to acquire a capital asset. Id. Additionally, taxes imposed to pay for improvements only benefiting the property assessed are also not deductible as a tax. IRC § 164(c)(1); Treas. Reg. § 1.164-4(a); Rev. Rul. 75-455, 1975-2 C.B. 68. However, similar to a tax on rent, such taxes for a local benefit may be deducted under section 162 as an ordinary and necessary business expense, provided the requirements of section 162 are satisfied.

In the case of County Bill 34-90 as drafted, the proposed tax is not deductible under section 164 as it would be incurred in the acquisition of property, and accordingly must be added to the tax basis of the property under section 164(a). The same tax would not be deductible under section 162 as the tax is a one time tax for a construction permit and therefore provides a benefit beyond the current tax year, and is expended to acquire a capital asset.

An Alternative

As I understand from the background materials you provided, the goal of County Bill 34-90 is to raise revenue from new construction buildings to assist the County in paying for infrastructure improvements and overall costs attributable to growth. The tax as currently proposed seeks to raise $5.00 per square foot from newly constructed buildings after exempting the first 1200 feet of any construction project. This would exempt an individual building an addition on the family home, while still taxing small construction projects.

there are funds available to pay the tax. Although the building or addition may be fully constructed, until the time in which the property is leased, occupied or sold there is no growth impact to the County as the asset has yet to be place in service. Also, collecting the tax when the building or addition is generating revenue to the taxpayer, either through lease or sale, is more economic to the builder and would not otherwise deter economic growth in the County.

After you have had an opportunity to review the suggested revision to the bill, please do not hesitate to contact me at (415) 768-1674 if you have any questions or need any additional information.

Best Regards,

Mark A. Muntean

Mark A. Muntean
Senior Tax Attorney

cc: Craig L. McCarty, Vice President and Regional Manager, Bechtel Investments Realty, Inc.

Enclosure: As Stated

MEMO

THE MARYLAND-NATIONAL CAPITAL PARK AND PLANNING COMMISSION

TO: Ben Bialek, Attorney, County Council
Mike Faden, Attorney, County Council

VIA: Drew Dedrick, Chief, Research Division

FROM: Sally Roman, Planner, Research Division Sally

SUBJECT: Revenue Enhancement Measures - Construction Excise Tax

DATE: April 11, 1991

RESIDENTIAL - Excise Tax

1. Housing Unit Sizes

The attached tables present the gross square footage of a 400 unit sample of single-family housing, including detached and townhouse units, completed in Montgomery County in 1990. The data includes the mean, median, range, and distribution of sizes of townhouse, single-family detached, and all single-family housing including and excluding basements. The data was gathered from the Maryland Tax Assessor's files by Research Division staff. The basic files do not distinguish between cellars and basements; consequently, the term basement is used for both. Garages are not included in this data.

Based on the Tax Assessor's parcel file, the average gross floor area for all apartments in the County, regardless of year built, is 1,089 square feet. This figure is based on total floor area of apartment buildings divided by the total number of units. As a result, it includes not only the space in each unit but the common space as well. This type of measure is frequently used when discussing apartment development.

This data indicates that there were no single-family dwelling units of less than 800 square feet completed in the County in 1990 that appeared in the sample survey, and that the average apartment was almost 300 feet larger than the proposed 800 square foot figure.

It is generally agreed, by people in the housing industry, that the late 1980s were a period when the industry concentrated on building move-up housing. This housing responded to the strong demand largely generated by members of the baby boom generation as they entered their 40's, the typical age to purchase move-up housing. Move-up housing tends to be relatively large and fairly luxurious. The current economic downturn and signs of pent up demand for starter and smaller housing may mean that houses built in the next few years will be smaller and simpler.

2. Housing Cost Implications

The following tables are intended to illustrate the implications of a development tax on residential construction. A $3.75 per square foot tax has been applied to the median sized unit for each type of housing after subtracting an 800 square foot exemption in the first table and 1,200 square feet in the second.

Development Tax on a Median Sized Unit
with a 800 Square Foot Exemption

Unit Type	With Basement	Without Basement
All Single-Family	$7,995	$4,560
Single-Family Detached	$11,580	$6,761
Townhouse	$4,905	$2,303

Source: Montgomery County Planning Department, Research Division, April 1991.

Development Tax on a Median Sized Unit
with an 1,200 Square Foot Exemption

Unit Type	With Basement	Without Basement
All Single-Family	$6,495	$3,060
Single-Family Detached	$10,080	$5,261
Townhouse	$3,405	$803

Source: Montgomery County Planning Department, Research Division, April 1991.

Economic theory says that a development tax will be shared between the buyer and seller of a housing unit in varying proportions depending upon market forces. To illustrate the "worst case" impact of a tax, assume that the buyer had to pay the entire tax. Under those circumstances, the Planning Department's Affordability Index for housing using 1989 prices and income would decrease from 69 on a base of 100 for the median single-family house, attached and detached, to 66 with a 1,200 square foot exemption and 63 with an 800 square foot exemption. This index shows the relationship between median household income and median housing prices. When the index is 100 the household with the median income can afford to purchase a median priced house. An index in the 60s means a serious imbalance between median income and median price.

Attachment

Table 1

Mean, Median and Range of Gross Floor Area of Single-Family Houses Completed in 1990 in Montgomery County

(in Square Feet)

	Mean	Median	Range Low High
Single-Family Detached, Basement	4,271	3,888	1,960-19,572
Single-Family Detached, Excluding Basement	2,892	2,603	1,320-13,048
Single-Family Attached, Basement	2,108	2,040	1,335-2,016
Single-Family Attached, Excluding Basement	1,414	1,360	900-3,024
All Units, Basement	3,316	2,932	1,335-19,572
All Units, Excluding Basement	2,239	2,016	900-13,048

Note: Basement means basement or cellar.

Source: Montgomery County Planning Department, Research Division, and Maryland State Tax Assessor, April 1991.

Table 2

Gross Square Footage of Single-Family Houses
Completed in 1990 in Montgomery County

Number of Units by Square Feet

Square Feet	Single-Family Detached Without Basement		Single-Family Detached With Basement		Townhouse Without Basement		Townhouse With Basement	
< 800	0	0%	0	0%	0	0%	0	0%
800-999	0	0%	0	0%	8	5%	0	0%
1,000-1,199	0	0%	0	0%	7	4%	0	0%
1,200-1,399	1	0%	0	0%	92	53%	8	5%
1,400-1,599	0	0%	0	0%	42	24%	0	0%
1,600-1,799	17	8%	0	0%	6	3%	7	4%
1,800-1,999	9	4%	1	0%	9	5%	63	36%
2,000-2,199	24	11%	0	0%	10	6%	53	30%
2,200-2,399	26	12%	0	0%	0	0%	19	11%
> 2,400	143	65%	219	100%	0	0%	24	14%

Note: Basement means basement or cellar.

Source: Montgomery County Planning Department, Research Division, and Maryland State Tax Assessor, April 1991.

GROWTH OF IMPACT FEES CONTINUES. The use of impact fees is spreading and the amount charged is rising, according to a recent study of 33 jurisdictions nationwide conducted by the Growth Management Studies Center at the University of Florida. The average impact fee for residential use was $3,001 in 1990, 39 percent higher than in 1988. Over the two-year period, industrial development fees increased 80 percent—the average 1990 fee was $968 per 1,000 square feet in a facility. Office development fees increased 50 percent, to $2,165 per 1,000 square feet, while retail development fees increased 17 percent, to $3,321 per 1,000 square feet. The highest impact fees were found in California, where fees are levied of over $15,000 per single-family house. (*Zoning News*, December 1990; American Planning Association, 1313 E. 60th Street, Chicago, Illinois 60637; 312-955-9100.)

National Average Impact Fees: 1990

Type of Impact Fee	Single-Family Home per Unit	General Industry per 1,000 Sq. Ft.	General Office per 1,000 Sq. Ft.	General Retail per 1,000 Sq. Ft.
Road	$1,547	$800	$1,840	$2,281
Parks	526	no fee	no fee	no fee
Public Facilities	95	37	87	115
Police Protection	53	55	89	103
Fire Protection	135	76	149	222
Library	86	no fee	no fee	no fee
Schools	559	no fee	no fee	no fee
TOTAL	$3,001	$968	$2,165	$3,321

Source: *Growth Management Studies Newsletter*, June 1990.

National Average Impact Fees: 1988

Type of Impact Fee	Single-Family Home per Unit	General Industry per 1,000 Sq. Ft.	General Office per 1,000 Sq. Ft.	General Retail per 1,000 Sq. Ft.
Road	$1,009	$427	$1,230	$2,526
Parks	223	no fee	no fee	no fee
Public Facilities	107	33	82	130
Police Protection	51	49	79	111
Fire Protection	76	29	50	70
Library	90	no fee	no fee	no fee
Schools	606	no fee	no fee	no fee
TOTAL	$2,162	$537	$1,441	$2,837

Source: *Growth Management Studies Newsletter*, June 1990.

REGIONAL DISTRIBUTION CENTERS GROW IN POPULARITY. Continuing increases in labor costs and coincidental advances in technology are leading many firms to consider streamlining their operations by using a regional distribution center. Firms are designing and implementing buildings to maintain or improve delivery time from greater distances, to ensure careful control of inventory, and to realize cost-effective development solutions. These highly automated centers are usually located outside of major urban areas and geared to broad geographic areas. They feature 30-foot-high ceiling clearances, flexible rack and storage setups, sophisticated bar-coding systems, and computerized location and dispatching systems. Metropolitan areas projected to have vastly increasing needs for additional bulk distribution space include Los Angeles; Metropolitan New York/New Jersey; Chicago; San Francisco; Miami/Fort Lauderdale; Detroit; Philadelphia; Atlanta; Washington, D.C.; Dallas/Fort Worth; Boston; Seattle; Houston/Galveston; Minneapolis/St. Paul; and Milwaukee/Racine/Sheboygan. (*Development Magazine*, National Association of Industrial and Office Parks, 1215 Jefferson Davis Highway, Suite 100, Arlington, Virginia 22202; 703-979-3400.)

Land Use Digest

Published monthly by ULI–the Urban Land Institute, 625 Indiana Avenue, N.W., Washington, D.C. 20004-2930. David E. Stahl, Executive Vice President; Frank H. Spink, Jr., Staff Vice President, Publications. Subscriptions (@ $15) available only to ULI members and associates; cost included in annual contributions. Second class postage paid at Washington, D.C. Postmaster, send address changes to the Urban Land Institute. *Land Use Digest* is cataloged as ISSN 0023-765X.

Editor . . . . .Nancy Minter
Managing Editor . . . Nancy Stewart
Manager, Computer-Assisted Publishing . . . Helene Y. Redmond

Publications cited in *Land Use Digest* are not available through ULI; they can be obtained from sources listed.

May 13, 1991

MEMORANDUM

TO: County Council

FROM: Michael Faden, Senior Legislative Attorney

SUBJECT: Estimates of cost of construction excise tax to new homebuyers

Several letters to the Council on Bill 34-90, the construction excise tax, have included versions of the attached table. It attempts to estimate the cost to an average homebuyer of the construction excise tax, spread over the period of owning the home.

For the following reasons, this table does not present an accurate picture. In my view, it goes beyond even a worst-case scenario.

— It assumes the builder will pass all its costs through, and that the builder does not face any competitive pressure to hold costs down.

— It assumes commissions and fees are paid to third-party brokers, insurers, and lenders, rather than ones affiliated with the builder. Commissions and fees paid to the builder's affiliates need not increase the builder's construction loan.

— It assumes all taxes are financed, and none are paid out-of-pocket by the buyer or the seller.

— It assumes that the homeowner will own the home (and pay these costs) for 30 years, rather than selling it in the average 5-7 year time.

— It ignores the homeowner's ability to recoup these costs when selling the home.

— It assumes that the homeowner did not sell an existing home before buying this one. If the homeowner did sell an existing home, he or she probably benefitted from the increase in value of that home, if any, attributable to the higher prices caused by the excise tax.

— Most critical, it completely ignores the effect of the federal mortgage interest and property tax deductions. These would reduce the net impact of the excise tax on the homeowner, accepting all other elements of the attached table, by 33-37%, depending on the homeowner's tax bracket.

Finally, an arithmetic error (in the calculation of annual interest on page 2) that adds $373.80 to the 30-year total should be corrected.

Proposed Excise Tax on New Construction

Calculation of Tax

2,000.00	square foot house
- 1,200.00	square feet exempted
800.00	square feet to be taxed
x 3.25	construction excise tax per foot
$2,600.00	excise tax that builder must pay up front

Increased Costs on Builder's Construction Loan

$ 52.00	2 points to lender on $2,600 loan increase
11.44	State Revenue Stamps of $4.40 per 1,000 to record construction lender's deed of trust on $2,600 loan increase
4.55	Increase in Mortgagee's insurance policy at $1.75 per 1,000 on $2,600 loan increase
$2,667.99	Total Construction Borrowing increase (assuming tax is 100% financed)
266.80	Interest at 10% for 1 year on construction loan increase
$2,934.79	Subtotal Increase in House Price
176.09	6% Brokers Commission on $2,934.79
$3,110.88	Increase in Purchase Price Shown on Buyer's Settlement Statement[1]

Settlement Charges Increase

$ 31.11	1% Mont. County Transfer Tax on Purchase Price
15.55	1/2% State Transfer Tax on Purchase Price
13.69	$4.40 per 1,000 State Revenue Stamps on Purchase Price
6.22	$2.00 per 1,000 for Owner's title policy on Purchase Price
56.00	2 points to lender on loan increase (based on 90% loan and 10% cash down)
$ 122.57	Increase in Settlement Charges

Totals at Settlement

$ 122.57	Increase in Settlement Charges
311.09	Increase in 10% cash down
$ 433.66	Increase in Buyer's cash needed at settlement
2,799.79	Increase in Loan Amount
$3,233.45	Total Increase to Homebuyers at settlement

[1] *Assumes no mark-up in costs for builder profit, overhead, marketing, etc.*

Cost over 30 years to Homebuyer

Financing

Increase in loan amount of $2,799.79 at 10% on 30-year mortgage =

$ 24.37	per month
$ 292.44	per year
$8,773.20	over 30-year life of loan

Real Estate Tax

$3,110.22	increase in Purchase Price
x 40%	
x 3%	
37.33	per year
x 30	years
$1,119.92[2]	

Total Cost to Homebuyer over 30 years

$ 433.66	Increase in Buyer's cash needed at settlement
8,773.20	Increase in Buyer's financing cost
1,119.92	Increase in Buyer's real estate taxes
$10,326.78	TOTAL

[2] *Assumes constant 1991 dollars*

Letters

Does the council want to leave dire legacy?

6-11-91

Editor, *The Journal*:

If things were not bad enough already in the commercial and residential building business, the County Council is in the process of delivering the crowning blow. The construction excise tax — $10,000 on a medium-sized single-family home — which was tentatively approved by the County Council, will cripple the already wounded real estate industry beyond the point of recovery.

One has to wonder if our elected officials have lost complete touch with the real world. Anyone who reads the paper, hears the news or has experienced this recession firsthand knows that similar excise taxes have all but "shut down" certain segments of the economy, such as the automobile and boating industries.

One may argue effectively for excise taxes on "luxury items." I will argue louder and longer that housing is not a luxury! Shelter is a necessity, and the idea of slapping a construction excise tax on a purchase as critical — and as expensive — as a home is darn near immoral.

It burns me to hear council members talk from both sides of their mouths! No doubt you have heard the lip service paid to the cause of affordable housing. Developers and private enterprise have been urged continually to take an ever-greater responsiblity for providing shelter for low- to moderate-income families. The council professes sadness over the high cost of teachers, firefighters and police. Yet their concern is belied by the excise tax bill, an exclusionary piece of legislation that will most certainly deny many of their ability to live in Montgomery County. I charge the council of shedding crocodile tears.

It is clear to me that the excise tax bill is a smoke screen for the County Council's deep no-growth sentiment. I contend that playing political games with people's livelihood and quality of life to "better" one's chances of re-election is not only selfish, it's ultimately self-defeating. This is a measure by which everyone, sooner or later, will lose.

By taxing new homeowners, many of our children will be excluded from living in the county of their birth. Many service-sector workers will be forced to leave Montgomery County and then commute to and from their Montgomery County jobs, adding to the already critical problems of highway congestion, automobile pollution and excessive fuel consumption.

Housing will cost more almost immediately — yet only a portion will be passed along to the already-strapped consumer. The balance of the excise cost would normally be absorbed by the builder, but the profit is already gone from the home-building business.

Higher housing costs, a weakened employment base, road congestion, environmental impact, more and more businesses forced into bankruptcy — is this the legacy the County Council hopes to leave behind?

CLARENCE E. KETTLER
Kettler Brothers Inc.
Montgomery Village

48

Developers here have gotten off pretty easy

Editor, *The Journal*: 6-18-91

Developer Clarence Kettler just can't accept the fact that Montgomery County taxpayers no longer are willing to subsidize developers' profits (letter, June 11).

Under the four-year regime of previous county executive Sidney Kramer, Mr. Kettler and others built their developments, pocketed their profits and left the rest of us to pay the huge costs that development incurs.

During Mr. Kramer's administration, we collected about $10 million in impact fees and allowed developers to contribute $70 million to buy their way out of building moratoriums when road capacities were saturated.

Yet, during that period, we ran up $1.7 billion in costs for roads, schools, libraries, police stations — the infrastructure that follows development.

As County Executive Neal Potter and several council members have said, if we'd had a development tax when it was proposed four years ago, we would be $200 million ahead now instead of $185 million behind.

The council soon will pass a modest development tax. It means that an average-sized, 2,000-square-foot house will bear a tax of $3,000. This need not add to the home buyer's cost. House prices are set by the competitive market, and there are plenty of existing houses for sale in Montgomery County today, many of them in the $200,000 range.

County developers should be relieved at how lightly they're getting off. We're behind other jurisdictions.

In a nine-state survey made a few years ago by James Nicholas of the University of Florida, the development tax on a house averaged $3,686. According to the same formula, retail buildings were being taxed as high as $11,260 per 1,000 square feet of building.

As expert Douglas Porter of the Urban Land Institute says: "The message to developers is: If you want to play the game, you will be expected to pay something."

NORMAN KNOPF
Bethesda

WEST GROUP

91 JUL 25 A8:08

July 24, 1991

B 34-90

8:25
7-25-91
MF
CC
MM

Isiah Leggett, President
Montgomery County Council
Executive Office Building
101 Monroe Street
Rockville, Maryland

Dear Mr. Leggett:

Our understanding is that the Council will further discuss Bill 34-90 at an afternoon session on Thursday, July 25, 1991.

We have reviewed Mr. Potter's July 12, 1991 memo and quite frankly were pleasantly surprised that Mr. Potter is willing to collect the entire excise tax upon issuance of Certificate of Occupancy and that he recognizes the time the tax is least painful is at the time there is an income stream created. This obviously is an improvement over the previous proposal for 50% at building permit/50% at occupancy. It is unclear to us at this time whether occupancy is a one time event or whether payment will occur with each occupancy in a multi-tenant building. Of course our preference is with each use and occupancy permit as opposed to "shell" occupancy. The building, particularly in the current market, could be complete but unleased for some time. In keeping with Mr. Potter's premise that tax should be paid when a transaction takes place, we ask that some consideration be given to phased occupancy of an office building as opposed to a one time closing on a home.

The only other issue we implore you to reconsider is the $4.00 rate for offices. Yes, it is down from the $5.00 originally proposed, but be reminded that the $4.00 figure represents Mr. Adams' attempt to solve the core factor dilemma. He recognized that an office building has an unleaseable core (common area, stairwells, etc.) of 10 - 30%, probably 20% on average. Councilman Adams therefore suggested that rather than dealing with variable core factors, reduce the $5.00 proposal by 20% or $1.00, and tax 100% of the building. We view the reduction from $5.00 to $4.00 as a prudent and equitable answer to core factors, but the $4.00 figure is still too much. We have provided the Council with evidence that shows what the excise tax does to our competitiveness with neighboring Prince Georges County. We explained that whether the number is $5 or $4 or $3, the excise tax, unlike current impact tax, has never been quantified (CIP budget ⁄ sq. ft. of commercial or houses = tax).

WEST GROUP, Inc. 1600 Anderson Road, McLean, Virginia 22102. 703/356-2400

SC

Isiah Leggett, President
page 2
July 24, 1991

The Council has determined that proceeds of the tax will never go into the general fund. We support that decision, but as a result, the excise tax cannot be quantified a "budget balancer." The dollars are earmarked for Housing Initiative and Transportation Infrastructure only. But other than the Housing Initiative, the use of the money has not been related to costs required to implement specific transportation projects. Instead, the tax creates a "pot of money." The $3.00/$4.00/$2.40 for apartments, office and retail, and R&D respectively are merely feel good numbers. Can't you feel just as good with $3.00 for office? Wouldn't an across the board rate of $3.00 be less discriminating (i.e. we like housing, we hate offices, we love R&D), and more easy to implement.

We empathize with your housing and infrastructure dilemma, but WEST*FARM built or committed to build their area infrastructure consistent with their zoning and density. They then were subjected to APFO loophole closure and I-3 text amendments. They then agreed to limit their density even further. They are currently paying impact taxes which are quantifiable and tied to specific CIP infrastructure in Eastern Montgomery County. All we are asking for is equity and a sense of fair play. While we are realistic and know this Excise Tax is a foregone conclusion, we merely ask you to feel good about $3.00 a square foot for office rather than $4.00.

Very truly yours,

WEST*GROUP, Inc.

Thomas D. Fleury

Thomas D. Fleury
Vice President
Development Services

cc: William Kominers
Gene Lynch
Council Members

The Johns Hopkins University

Montgomery County Center
Edgar E. Roulhac, Ph.D., M.P.H.
Assistant Provost
Director, Montgomery County Center

91 JUN 19 P1:30

MF
cc

3H-90

June 19, 1991

The Honorable Isiah Leggett
President
Montgomery County Council
Stella Werner Office Building
100 Maryland Avenue
Rockville, Maryland 20850

004772

Dear Councilman Leggett:

Please allow me to share with you our concerns regarding an issue which, quite literally, threatens to penetrate to the very core of Johns Hopkins' future teaching and research presence in Montgomery County. Our concerns evolve around the Montgomery County Council's recently proposed excise tax on new construction.

Fundamentally, our concerns are that your recently proposed excise tax on new construction: [1] clearly exempts the University of Maryland as a State institution, [2] unfairly disadvantages Johns Hopkins University in comparison to the University of Maryland in Montgomery County, [3] raises, precipitously and harmfully, the costs associated with Johns Hopkins' agreement with Montgomery County to respond to the needs of its corporate and professional work force by providing future teaching and research opportunities and facilities at our Montgomery County Center, and [4] changes our previously written agreements with Montgomery County.

As you know, The Johns Hopkins University Montgomery County Center campus is the result of a collaborative association with the Montgomery County Government which invited the University to participate in the expansion of higher education opportunities for adults living and working throughout the area.

Since the establishment of Hopkins' advanced graduate academic presence in Montgomery County in 1986, course enrollments have accelerated from 500 to, now, more than 4,000. Course offerings have risen from 30 to nearly 300. Within the same time frame, the number of Hopkins' Schools offering programs at the Center have increased from one to three, and, today, include our world famous School of Public Health, our nationally acclaimed G.W.C. Whiting School of Engineering, and our professionally renowned School of Continuing Studies -- the graduate business and education arms of the University. The number of complete degree programs we offer in Montgomery County which are approved by the Maryland Commission on Higher Education has increased from three to ten. Each program is

(301) 294-7000
9601 Medical Center Drive
Rockville, Maryland 20850

made available in its entirety to professionals who wish to study on a part-time basis in a high quality learning environment which is located close to home or work. Additional programs will soon be instituted.

The County's initial vision that having a major research university in the area would be critical for future economic stability and community development continues to be confirmed by the growing acceptance of our academic programs and community services. However, this vision now seems to be threatened, as does Montgomery County's truly unique and stable multi-institutional educational partnership.

To summarize, in view of the concerns cited above we would deeply appreciate receiving your assistance and cooperation, and that of the entire Montgomery County Council, in securing an exemption for not-for-profit educational and research activities from the recently proposed excise tax on new construction.

Thank you ever so much for considering this request, and please accept my very best wishes and warmest personal regards.

Sincerely,

Edg- E. Raun

CC: Dr. William C. Richardson, Dr. M. Gordon Wolman, Dr. Eugene Sunshine, Ms. Janet Johnson, Ms. Annie Kronk, Mr. Frederick Savage; The Honorable Neal Potter, The Honorable William Hanna, The Honorable Bruce Adams, Mr. Jon Gerson, Mr. Clifford Kendall, Dr. Walter Plosila, Mr. Howard Thomas.

MONTGOMERY COUNTY
HIGH
TECHNOLOGY
COUNCIL,INC.

51 Monroe Street, Suite 1701, Rockville, MD 20850 (301)762-6325

RECEIVED COUNCIL

91 JUL 2 P1:35

July 1, 1991

The Honorable Isaiah Leggett
President
Montgomery County Council
Stella Werner Office Building
100 Maryland Avenue
Rockville, Maryland 20850

B 34-90

004995

MF
cc

IN FILE

Dear Councilman Leggett:

I am writing to request the correction of an inequitable aspect of the proposed construction excise tax that may inadvertently damage the prospect of continued development of higher education resources in Montgomery County.

It is our understanding that private higher education institutions in the County will be subject to the proposed construction excise tax (at a lower rate than commercial ventures), whereas public education institutions will be entirely exempt. Our concern lies directly with the impact that such a tax would have on the development of the facilities and programs of The Johns Hopkins University at its Shady Grove campus.

As you know, the High Technology Council has been working actively with both Johns Hopkins and the University of Maryland to develop their facilities and programs to benefit both the high technology community and the community at large. Our efforts in this regard have been spectacularly successful. Johns Hopkins enrollments have reached 4,000 this year at their Montgomery County Center building, which is operating at near capacity. They have been actively seeking funds to construct a second facility to meet the demand that exists.

The High Technology Council has just completed a second higher education needs assessment survey, a copy of which I am enclosing. The results clearly indicate that the amount of the unmet demand for higher education programs remains huge. Johns Hopkins and Maryland are actively working to bring the needed programs to Montgomery County residents and employees.

The proposed construction excise tax, if applied to Hopkins, would increase the cost of construction and needlessly hinder its ability to augment its programs here. Such a tax would be conterproductive to the best interests and express wishes of the County Government and its citizens when it requested that Hopkins commit itself to bring its programs here.

Another reason this tax should not be levied on Johns Hopkins is that it creates an unfair comparative disadvantage in relation to its public sector counterparts in the area, particularly the University of Maryland. Given the larger subsidies already afforded public institutions, it hardly seems fair to add a further financial onus on Johns Hopkins.

The High Technology Council therefore strongly urges the County Council to exempt from the proposed construction excise tax private higher education institutions in the County. It is our understanding that, under our proposal, only two institutions would be added to the list of exemptions--Johns Hopkins and Columbia Union College. Consequently, the fiscal impact of this revised exemption would be minimal.

Thank you for your consideration of this matter.

Sincerely,

Clifford Kendall

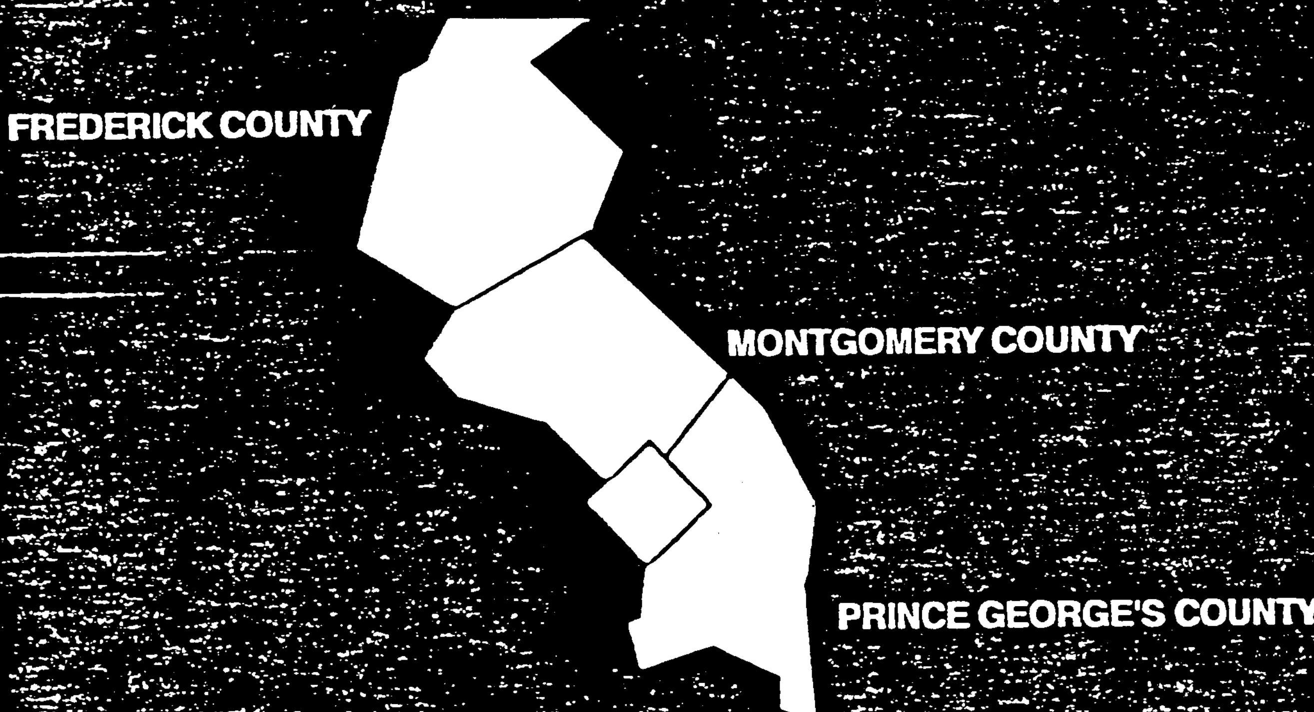
Clifford Kendall
Chairman

cc: County Council members
Hon. Neal Potter
Mr. John Gerson
Dr. Edgar Roulhac

Enclosure

REPORT ON THE SURVEY OF EDUCATIONAL AND TRAINING NEEDS OF EMPLOYEES OF REGIONAL HIGH TECHNOLOGY FIRMS

JUNE 1991



TECHNOLOGY

LINKING FREDERICK, MONTGOMERY & PRINCE GEORGE'S COUNTIES

2134-1

1180
6-4-91
N. Potter

Montgomery County Government

1991 JUN -3 PM 4:53

F41

MEMORANDUM

June 3, 1991

TO: Neal Potter, County Executive

FROM: Louis H. D'Ovidio, Director
Office of the Public Advocate for Assessments and Taxation

SUBJECT: Construction Excise Tax Exemptions

The discussion of the decision to include or exclude basements, cellars and garages as a part of the Construction Excise Tax has come to our attention and we feel compelled to insert our opinion.

It is our considered strong opinion that if the proposed legislation excludes or exempts areas such as basements, cellars and/or garages that it invites loopholes. A builder could decide to construct homes all with finished walk-out basements which would escape the tax but add significant value to the property. Similarly two and three car garages are value added. Why exempt garages when they could be considered a frill, not a necessity? Newly constructed houses with garages are generally higher value properties. Two or three car garages generally mean more cars and it may follow that they generate more trips than a lower value property.

The proposed exemption as applied to two example properties:

Example #1 - A total 1,600 square foot 3 level row townhouse (19'x28' each level) with no basement or garage. Walk in at street level. The first 800 square feet exempted - 800 square feet taxed. Approximate value range if located in Gaithersburg, is $100,000 - $115,000.

Example #2 - A total 1,600 square foot on main level detached 1-story house with 1,600 square foot walk-out basement finished or with the potential to be finished and a 400 square foot two car garage. The first 800 square feet exempted, an additional 2,000 square feet of basement and garage exempted, - 800 square feet taxed. Approximate value range, if located in Gaithersburg, is $270,000 - $290,000.

The proposed excise tax would be an identical $3,000 (800 sq.ft. x $3.75) on the two dwellings because of 800 square feet taxed in both cases. This potentially affects the cost of the moderately priced townhouse by a significantly higher percentage than the cost of the higher valued home because of the substantial difference in value basis. In the preceding example: $3,000 is 3.0% of the $100,000 valued townhouse, but only 1.1% of the $270,000 valued detached house.

If the primary goals of the proposed excise tax on new construction are (1) to create additional revenue to assist with infrastructure costs and (2) to do so in a reasonably equitable manner, it is our opinion that a system that could hit the lower priced houses the hardest is to be avoided, if possible.

We suggest that the total gross square footage including basement and garage space should be taxed (after exempting the first 800 square feet). This will create a situation where in the foregoing example the tax on the townhouse (800 sq. ft. @ $3.75) will remain at $3,000 or 3.0% of value, but the tax on the detached house (2,800 sq. ft. @ $3.75) becomes $10,500 or 3.8% of value.

We believe that the tax on the modestly priced unit should not be disproportionately higher in percentage terms than the tax on the higher priced home. The scenario that seems to help alleviate the disparity is a taxing of all of the square footage over 800. The scenario that appears to magnify the disparity is to exempt large amounts of basement and garage areas in addition to the 800 square feet.

Finally, if gross square footage less 800 square feet is taxed, it will be possible to create more revenue with a lower excise tax rate, thus further assisting the eventual purchasers of homes in the lower price range.

LHD:mjc

cc: William Hussmann
Gene Lynch
Richard Ferrara

RECEIVED ... STRAWBRIDGE RUN, INC.

P 34-90 91 MAY 7 A10:49

May 2, 1991

T/F cc

003903

Mr. Isiah Leggett, President
Montgomery County Council
Montgomery County Council Office
100 Maryland Avenue
Rockville, Maryland 20850

Re: Bill No. 34-90
<u>Construction Excise Tax Bill (the "Bill")</u>

Dear Mr. Leggett:

I am writing on behalf of Strawbridge Run, Inc., a not-for-profit corporation, formed to develop a continuing care retirement community for the elderly in Montgomery County. It has come to our attention that a bill is pending before the Montgomery County Council (the "Council") which would impose a graduated construction tax on developers of new construction projects. We understand that the proposed Bill does not directly address whether the construction of a continuing care retirement community would be subject to the construction tax.

We are submitting this letter to ask the Council to exempt the construction of continuing care retirement communities from the scope of the Bill. We understand that currently there are only a few continuing care communities approved for construction in Montgomery County and market realities probably would limit additional facilities in the future. Thus, the exemption would be very narrow. We believe that the economic loss to the County by granting this exemption for continuing care communities would be minimal. The impact on the developer of the continuing care community, however, would be dramatic. In our situation, the unanticipated costs that the Bill may add may make the project not economically viable. We believe that continuing care communities provide a valuable public service by furnishing housing and related amenities usually found in a residential community to the elderly. By exempting continuing care communities from the scope of the Bill, the community would be served by providing housing for the elderly and, because of the limited number of continuing care communities, the County should not be significantly affected by a loss of anticipated revenue from the Bill.

We would be pleased to discuss our request for an exemption for continuing care retirement communities from the Bill with the Council. I can be reached at the following address and telephone number: 12639 Knoll Road, Mt. Airy, Maryland 21771, (301) 831-3299. Thank you for your consideration of our request.

Very truly yours,

STRAWBRIDGE RUN, INC.

By: James P. Archibald
James P. Archibald, President

cc: Gilbert B. Lessenco, Esquire

LERCH, EARLY & BREWER
CHARTERED
LAW OFFICES

SUITE 380
3 BETHESDA METRO CENTER
BETHESDA, MARYLAND 20814-5367
TELEPHONE: (301) 986-1300

TELECOPIER: (301) 986-0332
TTY/TDD (301) 652-9354

HARRY W. LERCH
RONALD L. EARLY
ROBERT G. BREWER, JR.
ERIC M. CORE
GEORGE F. PAXTON
MARTIN J. HUTT
STANLEY J. REED
CINDI E. COHEN*
PAUL J. DI PIAZZA
R. DENNIS OSTERMAN*
RICHARD G. VERNON
JAMES L. BAER

RICHARD N. RUPRECHT
CYNTHIA M. BAR
THOMAS A. LERNER
LAURI EFF CLEARY
JANE E. DALRYMPLE+
LOUIS S. BONANNI
DONNA MORRIS DUVALL
SIGRID C. HAINES
SUSAN BERRY BLOOMFIELD
MARK S. ANTONVICH

OF COUNSEL
CHARLES L. WILKES
CONSTANCE B. LOHSE
ROBERT L. SALOSCHIN

EXECUTIVE DIRECTOR
RICHARD V. LITTLEFIELD
(NOT BAR MEMBER)

WASHINGTON, D.C. OFFICE
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SUITE 500
WASHINGTON, D.C. 20036-5004
(202) 293-5494

VIRGINIA OFFICE
9302 LEE HIGHWAY
SUITE 1100
FAIRFAX, VIRGINIA 22031
(703) 273-5911

ALL MEMBERS OF MD & DC BARS
EXCEPT AS OTHERWISE NOTED
*ALSO MEMBER VA BAR
+MD BAR ONLY

HENRY F. LERCH
1950-1986

WILTON H. WALLACE
1950-1959

WRITER'S DIRECT DIAL NUMBER:
(301)

September 20, 1991

Michael Faden, Esquire
Senior Legislative Attorney
Montgomery County Council
Stella Werner Council Office Building
100 Maryland Avenue
Rockville, Maryland 20850

Re: Construction Excise Tax

Dear Mike:

I have reviewed the latest draft of the Construction Excise Tax Bill and have some concern about the language regarding the effective date of the tax, which you changed from earlier versions of the Bill. I believe that you changed this in response to our conversation to clarify the application of the partial tax during the first year after April 1, 1992.

Section 2(a) of the Bill now states that it would apply to "any construction for which a building permit is issued on or after April 1, 1992." Previously, the Bill stated that it would apply when an application for a building permit was filed on or after April 1, 1992, such that building permits filed before this date would be exempt from the tax. Consequently, this grandfathering of permits applied for before April 1st has been deleted. This may have been done unintentionally in your attempt to clarify the effective dates of the Bill, since I do not remember any discussions indicating that permits which are pending on April 1st should be made subject to the tax. This would cause tremendous problems for DEP in processing applications. I hope the April 1st effective date for filing of applications can be put back in the Bill before the upcoming worksession.

Please call me at your convenience to discuss this change.

Very truly yours,

Harry

Harry W. Lerch

Taxcon20 B 9-17-91

CONSTRUCTION EXCISE TAX: REVENUE AVAILABLE FOR CIP

	FY 93	FY 94	FY 95	FY 96	FY 97	FY 98	Totals
Constr Tax Revenue	100	3,000	12,981	12,981	12,981	12,981	55,023
To Credits	15	450	1,947	1,947	1,947	1,947	8,253
To Admin Costs	85	365	100	100	100	100	850
To Housing Fund	0	2,185	5,000	5,000	5,000	5,000	22,185
Available For CIP							
With Housing	0	0	5,934	5,934	5,934	5,934	23,734
Without Housing	0	2,185	10,934	10,934	10,934	10,934	45,919

Notes:

1. This table assumes Executive proposal to collect at transfer or occupancy. Therefore, revenues are assumed to be received one year after permit application. Revenue is assumed to be nominal in FY 93 due to rush of permit applications to beat effective date of April 1, 1992. Revenue in FY 94 will be modest because of use of tax rates at 50 percent of stated level until April 1, 1993 and continued real estate recession. Revenue for FY 95-98 assumes latest Planning Department Intermediate Forecast of 4500 DU, plus 1 million sf of non-residential construction, per year on average.

2. Credits are for the existing Germantown and Eastern County impact tax and for the proposed Shady Grove Development District impact tax. Credits are assumed to be 15 percent of total revenue.

3. Administrative costs are assumed to be $300,000 for start-up information systems installation and $100,000 per year for regular operations.

4. The County Council has tentatively approved use of the first $5 million per year for the Housing Initiative Fund. The Executive opposes this concept. Therefore, revenues available for the CIP are shown with and without the allocation to the Housing Fund.

TAXCON19 8-14-91

CONSTRUCTION EXCISE TAX: COUNCIL RATES AND ESTIMATED REVENUE - FIVE YEAR AVG
(Revised Planning Dept Intermediate Forecast)

	Tax Per Building				Quantity of Construction		Tax Revenue
	SF	$	Actual $ / SF	% Constr Cost			
RESIDENTIAL							
Exemption	1200 SF				DU	4,500	$9,828,203
SFD	Rate / SF	$3.75				1,350	$7,181,460
Large	4,300	$8,045	$1.87	2.7			
Median	3,200	$4,836	$1.51	2.2			
Small	2,100	$1,627	$0.77	1.1			
TH	Rate / SF	$3.75				1,800	$1,971,742
Large	2,500	$2,794	$1.12	1.6			
Median	1,900	$1,043	$0.55	0.8			
Small	1,400	($416)	($0.30)	-0.4			
APT	Rate / SF	$3.00				1,350	$675,000
Large	1,400	$900	$0.64	0.9			
Median	1,000	$300	$0.30	0.4			
Small	700	$300	$0.43	0.6			
NON-RESIDENTIAL							
Exemption	1200 SF				SF	1,000,000	$3,152,500
Charitable Service & Schools							
	$1.00 per SF						
	40,000	$38,800	$0.97	1.0			
	20,000	$18,800	$0.94	0.9			
Warehouse, Mfg, R&D, Charitable Office							
	$2.40 per SF						
	80,000	$189,120	$2.36	3.9			
	40,000	$93,120	$2.33	3.9			
	20,000	$45,120	$2.26	3.8			
All Other	$4.00 per SF						
	80,000	$315,200	$3.94	3.9			
	40,000	$155,200	$3.88	3.9			
	20,000	$75,200	$3.76	3.8			
TOTAL REVENUE							$12,980,703

63

Notes to table: CONSTRUCTION EXCISE TAX - COUNCIL RATES AND ESTIMATED REVENUE

SFD = Single Family Detached, TH = Townhouse, APT = Apartment.

Median DU sizes are derived from Planning Dept. survey. Large is about one third bigger, Small is about one third smaller than Median.

Tax per building for SFD and TH assumes a building with three equal floors, one of which is a basement. For tax purposes, it is assumed that one third of basement is finished and taxable.

Tax per "building" for APT is tax per unit. The Median and Small units are smaller than the exemption of 1200 SF, so there is no tax on the units themselves. For all units, an average of 100 SF per unit is assumed for taxable common areas.

Construction cost is assumed to be $70/sf for residential, $60/sf for warehouse, and $100/sf for other non-residential.

Revenue for SFD = number of units X tax on Median unit X 1.10. The extra 10 percent reflects the fact that the mean house size is greater than the median.

Revenue for TH = number of units X tax on Median unit X 1.05. The extra 5 percent reflects the fact that the mean house size is greater than the median.

Revenue for APT = number of units X $500. The $500 assumes 100 SF per unit of of common area and some units larger than 1200 SF.

Revenue for Non-Residential assumes an average building size of 40,000 SF and an average tax rate of $3.25 per SF.

Montgomery County Government

MICHAEL E. FADEN
Legislative Counsel
Montgomery County Council

Stella B. Werner Council Office Building
Rockville, Maryland 20850
(301) 217-7905

Bill 34-90 Construction Excise Tax

Amendment by Councilmember Adams

Effective dates -- economic indicator study

On circle 10, lines 21 and 23, replace [[April 1, 1992]] with January 1, 1993.

On circle 10, line 23, replace [[April 1, 1993]] with January 1, 1994.

Add after §2(a) on circle 10, line 25:

(b) (1) The Council intends to have a construction excise tax in place when the economy recovers as an important element of a balanced, equitable package to fund infrastructure and ensure an appropriate supply of affordable housing. So that this tax will not hinder the economic recovery, the Council intends in June 1992 to review its effective date.

(2) By June 1, 1992, Council staff, with assistance from staff of the Planning Board and the Executive branch, must prepare a background paper on the state of the County's economy. This paper must review past and current economic indicators, including new housing unit completions, residential real estate transfers, and non-residential space completion, and project future levels of those indicators.

(3) The Council may, by resolution adopted by June 30, 1992, after a public hearing advertised under Section 52-17(c), defer the effective dates set in Section 2(a) to later dates.

Bill 34-90 Construction Excise Tax

Amendment by Councilmember Adams

Limit on support for federal or state projects

On circle 10, line 15, insert:

<u>Unless the Council by resolution directs otherwise, revenue from this tax must not be appropriated to any project that is eligible for federal or state funding, except for the County's matching share of the project costs.</u>

12-4

Montgomery Votes to Tax Residential Construction

Levy to Add $6,000 to Cost of Typical House

By Charles Babington
Washington Post Staff Writer

A sharply divided Montgomery County Council enacted a tax yesterday that will add thousands of dollars to the cost of new houses despite outcries from residential builders, whose industry has hit a 15-year low in the county.

The tax would amount to $6,000 on a typical detached house and $795,200 on a new office building, officials said. It will take partial effect in 13 months and full effect in 25 months. The reaction from builders, however, was immediate.

"It's unbelievable; it's unreal," said Thomas A. Natelli, president of the Montgomery Chamber of Commerce and head of a construction company. "Developers are closing up shop, filing for bankruptcy. It just amazes me that [council members] don't have an understanding of what the economic reality is."

The only Washington area jurisdiction with a countywide construction impact fee is Anne Arundel County; Howard County is contemplating one. Anne Arundel's rates, enacted four years ago, are considerably lower than those approved in Montgomery and apply equally to large and small houses.

Montgomery's tax is unusual because it increases with the size of the house. Although many local taxes on commercial construction are based on square footage, an officer of the National Association of Home Builders said he knew of no local government in the nation that taxes new houses in that manner.

The Montgomery council voted 5 to 4 against postponing the long-debated "construction excise tax," and then approved the bill 5 to 3. A similar measure narrowly failed in April 1990, when pro-business members controlled the council. In the 1990 election, however, voter resentment

See MONTGOMERY, A22, Col. 4

TAX ON NEW CONSTRUCTION
COST PER SQUARE FOOT*

Category	Effective 1/1/93	Effective 1/1/94
Single-family residential	$1.875	$3.75
Multifamily residential	$1.50	$3.00
Warehouse, manufacturing, research and development, nonprofit office	$1.20	$2.40
Office, retail, other nonresidential	$2.00	$4.00
Nonprofit care-giving facilities and private schools	$0.50	$1.00

*First 1,200 square feet of any building exempt.

Builders in Montgomery Call New Tax A Major Blow to Affordable Housing

MONTGOMERY, From A1

of overdevelopment helped sweep into office County Executive Neal Potter (D) and several council members who shared his strong support for the construction tax as a way to pay for the schools, roads and other services that growth requires.

"There have been endless excuses and alternatives put forward," newly elected council President Bruce T. Adams (D-At Large) said yesterday. By phasing the tax in for 1993 and 1994, he said, "it will be in place for the economic recovery that will come one day."

But other council members denounced the bill's timing.

"This is the worst possible thing we could do to [developers] at this time," said council member William E. Hanna Jr (D-District 3).

Gail Ewing, an at-large Democrat, said the new tax on developers amounted to "hitting them while they're down, pure and simple."

About 3,080 houses were built in Montgomery last year, the lowest total since 1976 and one-third the 1987 figure. Adams said the council will reexamine the tax's starting date next summer, and may delay it further if the construction industry remains depressed.

In May, county officials estimated that the new tax could generate about $20 million a year. Yesterday, however, council members said the tax would generate much less than that in today's depressed construction market.

Voting for the tax were Democrats Adams, Isiah Leggett (At Large) and Derick Berlage (District 5), and Republicans Nancy Dacek (District 2) and Betty Ann Krahnke (District 1). Several of them said the new construction tax is only one of the steps that eventually will be taken to raise money for new roads and other infrastructure needs.

NEAL POTTER
... strong supporter of building tax

Several developers said the burden should be shared by existing residents and businesses, which benefit from new roads and schools.

"The easiest person to go after is the non-existing constituent, and that's the new home buyer," said Robert Mitchell, president of C-I/Mitchell & Best Co., a Rockville-based residential builder. The new tax, he said, "drives the cost of housing up, and makes a mockery of [council members'] advocacy of affordable housing .... It shows a total lack of understanding of what the real-world economy is."

Mitchell said the tax, when fully implemented, would add $8,000 to $10,000 to the cost of the houses he builds, all of which will be absorbed by the buyer.

To encourage construction of small, lower-priced houses, the council agreed to exempt the first 1,200 square feet of any new building from the tax. For each remaining square foot of floor space, the fully implemented tax would be $3.75 for single-family houses; $3 for apartments and condominiums; $4 for office and retail buildings; $2.40 for warehouse, research and nonprofit spaces; and $1 for private schools and nonprofit health-care facilities.

The tax would not apply to garages. It would apply at half rates to legally habitable basements and attics. County officials said the fully implemented tax would be $117,120 for a 50,000-square-foot industrial park; $3.4 million for an 850,000-square-foot mall; $6,000 for a 2,800-square-foot detached house; $4,500 for a 2,400-square-foot town house; and $600 for a 1,400-square-foot apartment.

Hanna implored the council to wait and consider a new report by an advisory group consisting mainly of business executives who oppose the tax. The group recommended a new tax for all county residents, averaging about $91 annually per household, to help finance roads, schools and other public needs.

Natelli said the new tax would add $3,750 to $8,625 to the price of the 600 houses under construction in Milestone, a Germantown area complex his company is developing.

He said his company already had agreed to donate land for a county park and a school, and to make $15 million in area road improvements. "Who's going to tell my banker" that the new tax will add $2 million to the project's cost, Natelli said.

The council's vote, he said, "is unfathomable to me .... It's going to significantly raise the cost of homes, making Montgomery County more exclusionary in nature."

Kenneth Lambert/Journal

ght's hearing was jammed with both
ions and opponents of a spay-neuter bill.

MS- 12/4/91

New tax hammers builders, foes say

By MATT HAMBLEN
Journal staff writer

Over angry objections by recession-racked developers, the County Council yesterday approved a tax on almost all types of new construction.

The tax will take effect in 1993 and raise money for transportation projects and public housing. It imposes a $1 to $4 fee per square foot of new construction, with the first 1,200 square feet of each building or apartment exempted.

If the economy were normal, county officials said, the tax would raise between $10 million and $13 million a year, with the first $5 million reserved for public housing projects.

But critics say that given the dreary pace of construction in the county, the tax is not likely to raise much until the economy improves.

Several developers yesterday urged the council not to pass the construction tax. As an alternative, they suggested a transportation utility fee to be paid by all county residents and businesses.

The utility fee — which would be similar to

Please see TAX, A2

Opponents say tax hammers builders

TAX from A1

one being developed by officials in Orlando, Fla. — would spread out equitably the burden of paying for the transportation projects the county will need, the developers said.

The developers blasted the construction tax for burdening newcomers to the county who are fewer in number and less able to pay.

When times get better, the cost of the construction tax — about $7,500 for a large detached home — may be passed onto home buyers, several developers said.

But as long as the housing market remains depressed, developers will have to the eat the tax, some said.

The construction tax is "a bunch of crap," said Thomas A. Natelli, president of the county Chamber of Commerce and a county housing developer. He said it will be hard to get banks to finance his projects when the tax increases his development costs by about 15 percent.

In Germantown, where Natelli is building 600 homes in the Milestone tract, he says the construction tax will add about $3,500 to each home's cost — or about $2 million in all. Natelli said the economy will not improve enough by early 1993, when the first phase of the tax takes effect, to allow builders to raise home prices.

"The development industry understands that it needs to pay its fair share [for roads and other projects]," Natelli said. "But the council has no idea what effect this will have."

The council passed the tax 5-3, with council member Gail Ewing, D-at large, absent. Ewing said she left the room while the tax was considered "because I had nothing to contribute."

Ewing was disturbed that the council, by a 5-4 vote, rejected her earlier motion to delay action on the construction tax until July 1 because of the bad economy. Passing the tax now, Ewing said, is "to hit 'em [developers] while they're down."

Voting with Ewing to delay action — and later voting against the tax — were council members William E. Hanna Jr., D-Rockville; Marilyn Praisner, D-eastern county; and Michael Subin, D-at large. All urged the council to consider the transportation utility fee.

Voting for the tax were newly installed Council President Bruce Adams, D-at large, and council members Nancy Dacek, R-western county; Betty Ann Krahnke, R-Bethesda-Chevy Chase; Isiah Leggett, D-at large; and Derick Berlage, D-Silver Spring.

At Adams' prompting, the council delayed the date the measure will take effect from this April 1 to January 1993. Half the rates will go into effect then, the other half a year later.

Adams' amendment would allow the council to further postpone the tax if the economy hasn't perked up by next June.

Another last-minute change exempts all schools, instead of just colleges, from the tax.

Construction tax rates

Office, retail	$4.00 sq. ft.
Detached homes and townhouses	3.75
Apartment or Condo	3.00
Warehouse, manufacturing	2.40
Non-profit care-giving facility	1.00

Exemptions: Tax does not apply to the first 1,200 square feet of any building or each apartment in a multifamily building. Schools, religious buildings and mode rately priced dwillings are exempt.

Kevin Rechin/Journal

DEATH NOTICES

CARLSON MORRIS E. (ED)
Ed Carlson, 52 of Arlington, Virginia passed away December 1 while in the Shenandoah Mountains. After serving 22 years in the U.S. Navy, he had built a respected career in the defense community in Northern Virginia. He was a man of true wisdom, blessed with grace, a cherished friend to all who new him. His funeral will be held Thursday, December 5 at the BECKER FUNERAL HOME in Lawton, OK. In Lieu of flowers, the family would appreciate donations to the

Morris E. Carlson Memorial Fund
National Fish & Wildlife Foundation
1120 Connecticut Avenue
Suite 900
Washington, D.C. 20036

Dearest Ed,
As long as we can dream, as long as we have our memories, we will love you. As long as we have hearts to feel and imaginations to hold you, you will live beautifully forever.
C.P.

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County/State News

County Council passes excise tax despite warning

by Joseph C. Anselmo
Staff Writer

The County Council Tuesday approved a controversial development tax on commercial and residential construction, but delayed imposing the tax until 1993 because of the poor economy.

The council's 5-3 decision, aimed at raising funds for new roads and other infrastructure, drew howls from developers who wanted the vote delayed to study alternative proposals.

It also angered Councilwoman Gail Ewing (D-At Large), who walked out of the chamber before the vote.

"I think it was a travesty taking a vote today and I didn't want to be a part of it," she said. "We're talking about an industry that's in a depression, and we're hitting them while they're down."

Before passing the tax, the council narrowly defeated a proposal to delay the vote after hearing a report from a subcommittee of the Economic Advisory Council, an independent government advisory body.

The report, released late Monday, said a construction excise tax "will not generate enough money to be effective; it is neither reliable or predictable because it is dependent on development fluctuations."

The report suggested the council study alternative approaches, including a "Transportation Utility Fee," that could be based on the number of automobile trips a property generates.

Subcommittee member John H. Carman said the tax could amount to $91.25 a year.

Council President Bruce Adams (D-At large), who voted to proceed with the vote, promised Carman the council would still look into the recommendations.

In passing the tax, the council exempted the first 1,200 square feet of any building.

After that, new multi-family homes are levied at $3 per square foot, new single-family homes at $3.75 per square foot and new retail and office space at $4.

Buildings used primarily for higher education, religious purposes, or by non-profit educational institutions are exempt.

The Office of Management and Budget has estimated the tax could bring in $13 million annually when fully implemented.

Developers were skeptical.

"They (council) have no idea what this does in the way of revenue, it's cra said Thomas Natelli, a developer president of the Montgomery Co Chamber of Commerce.

Natelli said the county is requiring to pay $15 million in off-site road impro ments for 600 single-family homes h developing in Germantown's Milest project. The development tax, he s could cost an extra $3,500 per hous

"I've got to go to my banker and him we've just raised our developn costs by $2 million," he said.

Thomas Miller, president of a Bet da development firm, said the tax result in less tax revenue for the co because it will deter development.

"The bottom line is it takes two y to plan a project," he said. "You d know what to put into your calculatio