HB 1178

# Department of Legislative Services

Maryland General Assembly
2019 Session

## FISCAL AND POLICY NOTE
## First Reader

House Bill 1178 (Delegate Stewart, *et al.*)
Environment and Transportation and
Ways and Means

**Department of Housing and Community Development - Social Housing Act of 2019**

This bill establishes a Social Housing Program and Social Housing Fund within the Department of Housing and Community Development (DHCD). In fiscal 2021, the Governor must appropriate $2.5 billion in the annual State operating or capital budget to the fund. The bill imposes a 7.75% income tax rate on Maryland taxable income in excess of $1.0 million and requires that the Comptroller distribute the revenue generated from the income tax provisions to the Social Housing Fund established by the bill. **The bill takes effect July 1, 2019, and applies to tax year 2019 and beyond.**

## Fiscal Summary

**State Effect:** General fund revenues increase by $350.7 million in FY 2020 due to the income tax provisions; future years assume growth. General fund expenditures/special fund revenues increase correspondingly to capitalize the fund. General fund expenditures further increase by $1.5 million in FY 2020 for DHCD administration; future year administrative costs are covered with special funds. General fund expenditures and special fund revenues increase by an additional $2.5 billion in FY 2021 only due to the mandated appropriation. This analysis does not reflect expenditures and revenues related to any loans issued under the program. **The bill establishes a mandated appropriation for FY 2021.**

| ($ in millions) | FY 2020 | FY 2021 | FY 2022 | FY 2023 | FY 2024 |
|---|---|---|---|---|---|
| GF Revenue | $350.7 | $378.9 | $415.9 | $470.7 | $527.3 |
| SF Revenue | $350.7 | $378.9 | $415.9 | $470.7 | $527.3 |
| GF Expenditure | $352.2 | $2,878.9 | $415.9 | $470.7 | $527.3 |
| SF Expenditure | $0 | $1.8 | $1.9 | $2.0 | $2.0 |
| Net Effect | $349.2 | ($2,122.9) | $414.0 | $468.7 | $525.3 |

*Note: () = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate increase; (-) = indeterminate decrease*

**Local Effect:** Local governments and housing authorities are the only entities eligible for loans from the program to construct and operate social housing projects. To the extent that they receive loans, local revenues and expenditures increase significantly.

**Small Business Effect:** Meaningful.

---

## Analysis

**Bill Summary:** "Low-income household" and "middle-income household" mean one or more individuals who occupy the same residential dwelling unit and whose total household income meet specified limits established by the Secretary of Housing and Community Development for the program. "Social housing project" means a project eligible for financial assistance under the bill.

*Social Housing Program*

The stated purpose of the program is to (1) stimulate the construction of social housing; (2) increase and improve the supply of decent, safe, and sanitary social housing at affordable costs; and (3) support economic growth and activity by financing the construction of social housing projects. DHCD must (1) administer the program; (2) develop procedures to ensure that the projects receiving financial assistance from the program are in compliance with applicable occupancy restrictions; (3) use federal and State programs to help carry out the program; and (4) encourage the assistance or participation of local governments.

The Secretary of Housing and Community Development must set income guidelines for low-income households and middle-income households, as specified.

In administering the program, DHCD may act either directly or through the Community Development Administration (CDA). DHCD must adopt regulations to carry out the program that provide for (1) applications for money from the fund; (2) standards of eligibility, terms, and fees; (3) charges that must be imposed on program loans; and (4) the recapture of money of the fund from a borrower that does not use the money in a timely manner.

*Social Housing Fund*

The Social Housing Fund is a special, nonlapsing fund, administered by DHCD, for the purpose of supporting the development of social housing projects. The fund consists of:

- proceeds from the 7.75% tax levied on Maryland taxable income in excess of $1 million;
- money appropriated in the State budget;
- repayment of principal or payments of interest on loans from the fund;
- specified fees remitted to DHCD under the bill;
- interest earnings of the fund; and
- any other money from any other source accepted for the benefit of the fund.

The fund may be used only for the purpose of administering the Social Housing Program and making loans to approved applicants in accordance with the bill. Expenditures from the fund may be made only in accordance with the State budget.

*Program Loans*

Money in the fund may be used to make loans to an approved applicant to (1) acquire or construct a social housing project; (2) convert an existing nonresidential building or buildings to a social housing project; or (3) provide operating assistance to reduce the operating costs of a project by depositing the proceeds of the program loan in an interest-bearing account that is under the control of DHCD and is used to pay the operating costs, including the principal and interest when due, on any prior mortgage loan securing the project. A program loan may:

- be secured by a mortgage lien;
- be subordinate to other financing;
- have an interest rate as low as 0%;
- be payable out of surplus cash;
- be a deferred payment loan;
- provide for an equity participation by DHCD or contingent interest payable out of surplus cash or net equity; or
- have any other terms DHCD may require.

To facilitate the repayment of the program loan and achieve the purposes of the program, DHCD may modify the terms of the program loan, as specified.

If a program loan is secured by a mortgage, DHCD may (1) enforce the mortgage; (2) foreclose on the mortgage and take title to the mortgaged property or take deed in lieu of foreclosure; (3) convey title to a purchaser; (4) obtain and enforce a deficiency judgment; (5) allow assumption of the mortgage; and (6) contract with a private mortgage servicer to perform on behalf of DHCD any functions a servicer ordinarily performs. Without approval or execution by the Board of Public Works, DHCD may assign a mortgage for value or convey property after acquisition.

*Social Housing Projects*

A social housing project that receives funding under the bill must remain permanently in public ownership and may not revert to private or nonprofit ownership under any circumstances.

Rental units in a social housing project must be available to households of all income levels. A social housing project must include three tiers of rental units, with rental rates calculated as specified in **Exhibit 1**.

**Exhibit 1**
**Rental Rates for Units in a Social Housing Project**

| **Unit Tier** | **Components of Rental Rate** |
|---|---|
| Tier I | The estimated market rate for the unit. |
| Tier II | The unit's share of (1) operating costs for the social housing project, and any vacancy loss for the social housing project and (2) the unit's share of repayment costs for any municipal bonds or fund loans used to finance the project or, after any municipal bonds or fund loans have been repaid, a fee of at least 80% but not more than 100% of the amount previously charged. |
| Tier III | The rental rate for a Tier II unit, minus the difference between the rental rate for a Tier I unit and the rental rate for a Tier II unit. |

Source: Department of Legislative Services

Fees collected from Tier II units after any municipal bonds or fund loans have been repaid must be remitted to DHCD and deposited in the fund.

Generally, Tier III units must be made available only to low-income households, Tier II units must be made available only to low- and middle-income households; and Tier I units must be made available to households of all income levels. A social housing project must include (1) a minimum percentage of rental units reserved for seniors; (2) a minimum percentage of one-bedroom rental units reserved for individuals and couples; (3) an equal number of Tier I units and Tier III units; and (4) a number of Tier II units that is less than or equal to the combined number of Tier I units and Tier III units. Rental units restricted for occupancy to meet other federal, State, or local occupancy requirements may be counted toward the minimum requirements.

*Location Requirements*

A social housing project in an urban or suburban area must be (1) constructed at a high density relative to the county or municipality in which the social housing unit is located and (2) located within a reasonable walking distance of high-frequency public transit and quality schools, when available in the county or municipality.

*Eligible Applicants and Selection*

Only a political subdivision or a local housing authority may apply for a program loan. In reviewing an application for a program loan, DHCD must consider:

- the extent to which low- and middle-income households will be assisted by the proposed project;
- the number and percentage of low- and middle-income households currently living in the community where the project is proposed;
- the quantity, condition, and affordability of residential property in the community where the project is proposed;
- the economic feasibility of the proposed project;
- the degree of local government incentive and support provided to the proposed project, as specified;
- details of how any contractors or service providers will be selected for the project; and
- any other relevant factors.

In determining whether to award a program loan, DHCD must (1) deny an application that does not include a requirement that any contractor selected to work on the project pay the prevailing wage rate set for the locality by the Commissioner of Labor and Industry; (2) give preference to an application that prioritizes the use of unionized labor, cooperative or worker-owned businesses, and minority-owned businesses; and (3) give preference to an application that adds to the total available housing stock in a community.

*Prohibited Conduct/Penalties*

A person may not knowingly make or cause to be made a false statement or report in a document required to be submitted to DHCD under an agreement relating to a program loan. A loan applicant may not knowingly make or cause a false statement or report to be made to influence the action of DHCD on a program loan application or to influence action of DHCD affecting a program loan already made. A person who violates these prohibitions is guilty of a misdemeanor and on conviction is subject to imprisonment for up to five years, a fine of up to $50,000, or both.

*Income Tax Rate Increase*

Beginning with tax year 2019, the bill imposes a 7.75% income tax rate on Maryland taxable income in excess of $1.0 million. The bill requires the Comptroller for each tax year to estimate the income tax revenue attributable to the rate increase. The Comptroller must distribute the estimated amount to the Social Housing Fund by June 30, 2020, and each year thereafter. The bill also requires the Comptroller to waive any penalty or interest imposed on an individual relating to the payment of estimated income taxes for calendar 2019 to the extent that the Comptroller determines that the interest or penalty would not have incurred but for an increase in the income tax rates for calendar 2019 under the bill.

**Current Law:**

*Income Tax Rates*

**Exhibit 2** shows the State income tax rates under current law.

**Exhibit 2**
**Maryland State Income Tax Rates**
**Current Law**

| **Single, Dependent Filer, Married Filing Separate** | | **Joint, Head of Household, Widower** | |
|---|---|---|---|
| **Rate** | **Maryland Taxable Income** | **Rate** | **Maryland Taxable Income** |
| 2.00% | $1-$1,000 | 2.00% | $1-$1,000 |
| 3.00% | $1,001-$2,000 | 3.00% | $1,001-$2,000 |
| 4.00% | $2,001-$3,000 | 4.00% | $2,001-$3,000 |
| 4.75% | $3,001-$100,000 | 4.75% | $3,001-$150,000 |
| 5.00% | $100,001-$125,000 | 5.00% | $150,001-$175,000 |
| 5.25% | $125,001-$150,000 | 5.25% | $175,001-$225,000 |
| 5.50% | $150,001-$250,000 | 5.50% | $225,001-$300,000 |
| 5.75% | Excess of $250,000 | 5.75% | Excess of $300,000 |

Source: Department of Legislative Services

*Partnership Rental Housing Program*

DHCD administers the Partnership Rental Housing Program (PRHP), which is intended to expand the supply of affordable housing for low-income households. PRHP provides loans for rental housing that will be occupied by households with incomes at or below 50% of the statewide median. Loan amounts are limited to the greater of $75,000 per unit or the actual cost of the project. Projects financed through PRHP typically involve a partnership between State and local governments.

*Rental Allowance Program*

DHCD administers the Rental Allowance Program (RAP) to assist low-income households that are homeless or at risk of being homeless by providing housing assistance payments to (or on behalf of) eligible households. Under the program, the Secretary must establish (1) income limits for eligibility of low-income households that are up to 30% of the State or area median income, whichever is higher, and (2) minimum standards for eligible dwelling units. The Secretary must also establish the amount of payments that are made through RAP, taking into account specified factors.

Eligible uses of payments include rent, security deposits, utilities, and other housing-related expenses. DHCD may administer RAP by providing monthly housing assistance payments to (or on behalf of) eligible households directly or through political subdivisions, their local housing agencies or departments, or nonprofit organizations. DHCD is authorized to adopt regulations to carry out RAP, including timeframes for assistance and other appropriate criteria.

*Other Rental Assistance Programs*

DHCD is also authorized to establish and administer other rental assistance programs, including programs to assist households that (1) are homeless or at risk of homelessness; (2) include an individual with a disability or special need; (3) have been displaced or impacted by a disaster; or (4) have a critical or emergency housing need. DHCD's other programs are required to be administered in the same way as RAP. DHCD is required to consult with various other State agencies as well as units of local government when appropriate. The Secretary must establish criteria for the programs, including:

- income limits for households;
- timeframes for assistance;
- monthly assistance amounts;
- standards for eligible dwelling units, including types of units, inspection standards, and rent limits;

- eligible uses of assistance payments, which may include security deposits, utilities, and other housing-related expenses; and
- any other criteria the Secretary considers appropriate.

In establishing program criteria, the Secretary may consider factors that include:

- household size and expected average income;
- regional variation throughout the State;
- typical housing costs and expenses;
- relevant standards and definitions established for State and federal housing programs;
- housing needs of eligible households and the expected duration of the housing needs; and
- equitable distribution of funds statewide.

The Secretary is authorized to establish different criteria for different rental assistance programs.

**Background:**

*Social Housing, Generally*

Generally, the term social housing is used extensively in Europe to refer to government-owned or regulated affordable housing.

According to the U.S. Department of Housing and Urban Development (HUD), at the federal level, public housing was established to provide decent and safe rental housing for eligible low-income families, the elderly, and persons with disabilities. Public housing comes in all sizes and types, from single-family houses to high-rise apartments for elderly families. There are approximately 1.2 million households living in public housing units, managed by some 3,300 local housing agencies (HAs). HUD administers federal aid to HAs that manage the housing for low-income residents at rents they can afford. HUD furnishes technical and professional assistance in planning, developing, and managing these developments.

Eligibility for public housing is determined by income limits developed by HUD. HUD sets the lower income limits at 80%, and very low-income limits at 50%, of the median income for a county or metropolitan area. Income limits vary depending on the area.

*Rental Allowance Program*

DHCD advised for previous legislation that RAP provides grants to local governments to provide rent subsidies to low-income families who either are homeless or have an emergency housing need. The goal of the program is to enable these households to move from homelessness or temporary emergency housing into more permanent housing and to return to self-sufficiency.

Under RAP, eligible housing can include rooms, boarding house rooms, other single-room occupancy arrangements, apartments, group homes, transitional housing (but not temporary emergency housing), single-family houses, and mobile homes. Kitchen and bathroom facilities may be shared or independent. Motel and hotel rooms without access to kitchen facilities may be permitted if other more cost-effective and suitable housing is not available. Living facilities may be shared with other persons, including other program recipients. Housing may be furnished or unfurnished.

County governments, Baltimore City, and the City of Annapolis administer RAP by accepting applications from eligible residents, coordinating the program with other social services administered by the county, and providing staff links with CDA to ensure program requirements are being met. RAP is usually administered by the local social services office or the Section 8 agency (*i.e.*, public housing authority) or is contracted by the county to a nonprofit organization. Program funds are distributed to recipients throughout the State by formula. In fiscal 2017, RAP served 655 individuals.

**State Fiscal Effect:**

*Tax Revenues*

Beginning with tax year 2019, the bill imposes a 7.75% income tax rate on taxable income in excess of $1 million. The Comptroller's Office must distribute to the Social Housing Fund established by the bill the estimated revenue generated by the rate increase by June 30 each year. As a result, general fund revenues increase by an estimated $350.7 million in fiscal 2020 from the new tax rate; general fund expenditures and special fund revenues increase commensurately, reflecting the transfer of the tax revenues to the Social Housing Fund. **Exhibit 3** shows the projected State revenue increase resulting from the bill.

**Exhibit 3**
**Projected State Revenue Impact**
**Fiscal 2020-2024**
**($ in Millions)**

| FY 2020 | FY 2021 | FY 2022 | FY 2023 | FY 2024 |
|---|---|---|---|---|
| $350.7 | $378.9 | $415.9 | $470.7 | $527.3 |

Source: Department of Legislative Services

This estimate assumes that in each fiscal year, the Comptroller's Office distributes the revenues from one tax year. The actual revenue distributed in a fiscal year may be different given the schedule of tax payments made throughout the year, the effective date of the bill, and the required dates by which the Comptroller must transfer revenues.

*Mandated Appropriation and Social Housing Fund Activity*

General fund (potentially pay-as-you-go) expenditures and special fund revenues increase by $2.5 billion only in fiscal 2021 due to the mandated appropriation to the Social Housing Fund. The bill allows the funding to be included in either the operating or the capital budget, and expresses legislative intent that it be included in the capital budget. However, this analysis assumes that the appropriation is made from the operating budget for two reasons: (1) the General Assembly cannot mandate expenditures in the capital budget, and (2) the level of funding mandated far exceeds the State's debt capacity guidelines and is more than twice the level of the State's total annual capital budget. To the extent that the Governor includes the funding in the capital budget, bond revenues and expenditures increase commensurately in fiscal 2021, and special (Annuity Bond Fund) and/or general fund expenditures increase significantly in the out-years for debt service payments.

This estimate does not reflect expenditures from the Social Housing Fund related to any loans issued under the program beginning in fiscal 2021 following the receipt of revenues generated under the bill or the $2.5 billion mandated appropriation; the timing and magnitude of any spending from the fund is unknown. It also does not reflect special fund revenues from loan repayments and potential fee payments by recipients of the loans. It is assumed, however, that the Special Housing Fund operates as either a revolving loan fund or endowed fund, with future loans paid with a combination of tax proceeds, loan repayments, fees, and investment earnings.

*Administrative Expenses*

The general fund revenues generated under the bill are only available at the end of fiscal 2020, but DHCD must establish the program earlier so that it is prepared to begin making loans when the mandated appropriation is made at the beginning of fiscal 2021. Therefore, this analysis assumes that general fund expenditures increase by an additional $1.49 million in fiscal 2020 for DHCD to administer the program, which includes a 90-day start-up delay from the bill's July 1, 2019 effective date. As the bill allows the Social Housing Fund to be used for administration, expenditures to manage the program are then transferred to the special fund beginning in fiscal 2021, once the revenues from the new tax rate and mandated appropriation become available.

This estimate reflects the cost of hiring a total of 22 staff to develop and implement the program. Specifically, the estimate includes 1 program manager and 1 deputy program manager, 2 underwriting managers and 4 underwriters, 1 construction supervisor, 3 construction managers, 2 construction finance managers, 3 accountants, 2 loan processors, 2 administrative assistants, and 1 attorney to promulgate regulations, develop application and determination procedures, review, audit, and administer loans, and conduct outreach to eligible local governments to determine social housing financing needs. This estimate includes salaries, fringe benefits, one-time start-up costs, and ongoing operating expenses.

| | **General Funds FY 2020** | **Special Funds FY 2021** |
|---|---|---|
| Positions | 22 | 22 |
| Salaries and Fringe Benefits | $1,375,044 | $1,831,969 |
| One-time start-up Costs | 107,580 | 0 |
| Ongoing Operating Expenses | 10,313 | 13,750 |
| **Total State Expenditures** | **$1,492,937** | **$1,845,719** |

Future year expenditures reflect a transition to special fund support following the receipt of revenues generated under the bill, as well as full salaries with annual increases and employee turnover and ongoing operating expenses.

The Comptroller's Office incurs a one-time cost of $25,000 to modify its tax system to include the new tax rate. The Comptroller's Office further advises that it cannot implement the bill's provisions related to waiving interest and penalties without incurring a significant expense to modify its tax system. These costs are not reflected in this analysis.

The bill's penalty provisions are not anticipated to materially affect State finances.

**Small Business Effect:** Small businesses that are partnerships, S corporations, limited liability companies, and sole proprietorships may incur increased tax liabilities from the new tax rate for income that exceeds $1.0 million.

Any small businesses involved in the construction of social housing projects benefit from the funding provided for such projects under the bill. According to the U.S. Census Bureau, in 2016, there were 24,650 construction firms in Maryland that had less than 20 employees.

## Additional Information

**Prior Introductions:** None.

**Cross File:** None.

**Information Source(s):** Charles, Frederick, Montgomery, and Somerset counties; Maryland Association of Counties; cities of Frederick and Havre de Grace; Maryland Municipal League; Comptroller's Office; Governor's Office; Judiciary (Administrative Office of the Courts); Department of Budget and Management; Department of Housing and Community Development; Department of Labor, Licensing, and Regulation; Board of Public Works; State Department of Assessments and Taxation; U.S. Department of Housing and Urban Development; U.S. Census Bureau; Department of Legislative Services

**Fiscal Note History:** First Reader - March 11, 2019
an/mcr

Analysis by: Nathan W. McCurdy

Direct Inquiries to:
(410) 946-5510
(301) 970-5510