Department of Legislative Services

Maryland General Assembly
2010 Session

FISCAL AND POLICY NOTE

Senate Bill 285 (The President, *et al.*) (By Request - Administration)
Budget and Taxation

Smart, Green, and Growing - The Sustainable Communities Act of 2010

This Administration bill reestablishes the Heritage Structure Rehabilitation Tax Credit Program as the Sustainable Communities Tax Credit Program, transforms the program into a traditional tax credit program not subject to an annual appropriation, increases funding for the program by authorizing the Maryland Historical Trust (MHT) to award $50 million in credits in fiscal 2011 through 2013, and alters eligibility requirements for the program. The bill also makes several changes to other State programs, including the Community Legacy and Designated Neighborhood Programs.

Fiscal Summary

State Effect: General fund revenues decrease by $6.5 million in FY 2012 and by $18.5 million in FY 2015. State revenues decrease by a total of $72.0 million through FY 2017 as a result of extending the tax credit program. Special fund revenues and expenditures increase by $0.3 million annually in FY 2011 through 2014. General fund expenditures decrease by $5.0 million in FY 2011, by satisfying a contingent reduction in the proposed State budget.

($ in millions)	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015
GF Revenue	$0	($6.5)	($14.5)	($21.0)	($18.5)
SF Revenue	$.3	$.3	$.3	$.3	$0
GF Expenditure	($5.0)	$0	$0	$0	$0
SF Expenditure	$.3	$.3	$.3	$.3	$0
Net Effect	$5.0	($6.5)	($14.5)	($21.0)	($18.5)

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

Local Effect: Local highway user revenues decrease as a result of any credits claimed against the corporate income tax. Local expenditures are not affected.

Small Business Effect: The Administration has determined that this bill has a meaningful impact on small business (attached). Legislative Services concurs with this assessment.

Analysis

Bill Summary:

Sustainable Communities Tax Credit Program

This bill reestablishes the Heritage Structure Rehabilitation Tax Credit as the Sustainable Communities Tax Credit Program, transforms the program into a traditional tax credit program not subject to an annual appropriation, increases funding for the program by authorizing MHT to award $50 million in credits in fiscal 2011 through 2013. The program terminates October 1, 2013. The bill also expands and alters eligibility requirements for the program including allowing nonhistoric properties to qualify for the credit. Nonhistoric buildings, whether they are commercial or residential, can now qualify for a tax credit.

Although the bill is effective October 1, 2010, the bill's provisions apply to any rehabilitation of a single-family, owner-occupied residence and commercial property for which an application is received by MHT beginning July 1, 2010. The provisions of the Heritage Structure Rehabilitation Tax Credit will apply to rehabilitations for which applications are received by MHT before this date.

The tax credit may be claimed against the personal income tax, corporate income tax, and insurance premium tax. The value of the credit is dependent on the type of rehabilitation undertaken and is equal to (as a percentage of qualified rehabilitation expenditures):

- 20% for the rehabilitation of a single-family, owner-occupied residential certified historic rehabilitated structure;
- 25% for the rehabilitation of a certified historic structure that is a high-performance building (meets certain energy efficiency standards);
- 10% for the rehabilitation of a qualified rehabilitated structure; and
- 20% for any other qualifying rehabilitation.

The value of the tax credit may not exceed (1) for a commercial rehabilitation, $3 million or the maximum amount specified under the initial credit certificate; (2) for all other rehabilitations, $50,000. Except as provided below, if the tax credit exceeds the total tax liability payable by the person in the tax year, the unused amount may be carried forward for 10 tax years. The credit is refundable if: (1) the rehabilitation is a single-family, owner-occupied residence; (2) the rehabilitation is a commercial rehabilitation and the qualified rehabilitation expenditures do not exceed $250,000; or (3) the business entity is a nonprofit corporation and the qualified rehabilitation and the qualified expenditures do not exceed $250,000.

A qualified rehabilitated structure is a building that is located (1) in a transit-oriented development (TOD) district and is a commercial rehabilitation; (2) in a Main Street Maryland Community or a Maple Street Community; or (3) in fiscal 2012 in a sustainable community. The rehabilitation must be substantially rehabilitated and retain specified minimum percentages of internal and external walls and internal framework during the rehabilitation.

Residential Program

MHT can award an unlimited amount of residential credits for applications received through September 30, 2013. A single-family, owner-occupied residence is a structure occupied by the owner and the owner's immediate family as their primary or secondary residence. Single-family, owner-occupied residence includes a residential unit in a cooperative project owned or leased to a cooperative housing corporation and leased for exclusive occupancy to, and occupied by, a member of the corporation and the member's immediate family. Residences that are certified historic structures qualify for a credit of 20% of rehabilitation expenditures, otherwise the credit is equal to 10%.

Commercial Program

A commercial rehabilitation includes the rehabilitation of any building that is not a single-family, owner-occupied residence. MHT is authorized to issue $50 million in initial credit certificates to commercial rehabilitations and a maximum of $20 million in fiscal 2011, $15 million in fiscal 2012, and $15 million in fiscal 2013. A maximum of 40% of initial credit certificates can be awarded to qualified rehabilitated structures in each fiscal year. MHT may award initial credit certificates between October 1, 2010, and September 30, 2013.

MHT must for commercial rehabilitations adopt regulations establishing a rating system "based on past practices" that will fund projects that provide a stimulus for revitalization beyond the project and favors the award of tax credits based on seven criteria. Initial credit certificates will expire if (1) within 18 months after the certificate was issued, the applicant has not notified MHT that the rehabilitation has begun; or (2) within 30 months after the certificate was issued, the commercial rehabilitation is not completed. However, MHT may postpone the deadline for the completion of a project. The bill provides for recapture of the credit if within four years specified disqualifying work is performed or the property for which the credit is claimed is sold or otherwise transferred. The bill states that an initial credit certificate guarantees the business entity a tax credit under the provisions of the bill.

Tax Credit Administration

MHT is authorized to charge a reasonable fee necessary to certify historic rehabilitations and qualified rehabilitated structures. The fee imposed may not exceed 2% of the initial credit certificate issued for a commercial rehabilitation or qualified rehabilitation expenditures for a single-family owner-occupied residential rehabilitation. These fees are deposited to the Maryland Department of Planning Sustainable Communities Tax Credit Administration Fund established by the bill and are used to pay the costs of administering the credit established by the bill and the federal historic tax credit. MHT is required to notify the Smart Growth Subcabinet of applications and proposed awards prior to making the award of an initial credit certificate. By December 15, MHT is required to report specified information about the credit to the Governor, the General Assembly, and the Smart Growth Subcabinet.

The credit may be allocated among the partners, members, or shareholders of an entity in any manner agreed to by those persons in writing. The Comptroller may adopt regulations to require that an entity, other than a corporation, claim the tax credit on the tax return filed by the entity.

BRAC Revitalization Zones

Under current law, within 60 days after a submission date from an eligible local government, the Secretary of Business and Economic Development may designate one or more BRAC revitalization and incentive zones from among the areas described in the application. Before designating a zone, the Secretary is required to consult with the cabinet Secretaries or designees of the Maryland Department of Transportation (MDOT); the Department of Housing and Community Development (DHCD); the Maryland Department of the Environment (MDE); and the Maryland Department of Planning (MDP). The bill eliminates this required consultation and states that the Secretary of Business and Economic Development may designate a zone after receiving a recommendation from the Smart Growth Subcabinet.

Community Legacy and Designated Neighborhood Programs

The bill states that it is the intent of the General Assembly that these programs be used to create and support sustainable communities and be coordinated with other state programs such as the sustainable communities tax credit program established by the bill in order to maximize the State’s investment in sustainable communities.

Community legacy areas and community legacy plans are eliminated and replaced with sustainable communities and sustainable community plans. Under the community legacy program and neighborhood business development program, designated neighborhoods are eliminated and replaced as sustainable community designations. With this repeal, the authority of local governments to designate neighborhood communities is also repealed.

Sustainable community and sustainable community plan applications are to be sent to DHCD, and approved by the Smart Growth Subcabinet on recommendation of the Secretary of Housing and Community Development. In designating an area as a sustainable community, the Smart Growth Subcabinet must consider whether there is a need for reinvestment in the area and if: (1) entities in the including local jurisdictions support the proposed plan and have pledged resources to implement it; (2) the proposed plan addresses the need for reinvestment in the area and will enhance the area; (3) the community in the proposed area is culturally or historically significant; (4) the proposed area is near a town center or transportation center; (5) the proposed plan is consistent with other specified projects; or (6) there is a demonstrated need for financing assistance for small businesses, nonprofit organizations. In addition, DHCD can establish other standards by regulation, including standards established for other State or federal programs. To maintain a sustainable community designation, every five years an updated plan and application for approval must be sent to the Smart Growth Subcabinet. Any designated neighborhood approved by the Secretary of Housing and Community Development or community legacy area approved by the Community Legacy Board prior to October 1, 2010, will be considered a sustainable community for 18 months after the effective date of the bill.

A sustainable community is the part of a priority funding area that (1) is designated by the Smart Growth Subcabinet on the recommendation of the Secretary of Housing and Community Development; (2) has been designated as a BRAC revitalization zone; or (3) has been designated as a TOD district. The bill eliminates the Community Legacy Board and the advisory board to the Community Legacy Board.

Heritage Structure Rehabilitation Program

The bill allows heritage structure rehabilitation tax credits to be allocated among the partners, members, or shareholders of an entity in any manner agreed to in writing. This provision is retroactive and applies to any commercial rehabilitation project for which an application was approved by MHT after December 31, 2004. Any unencumbered funds in the Heritage Structure Rehabilitation Tax Credit Reserve Fund revert to the general fund on June 30, 2014.

Smart Growth Subcabinet and Transit-oriented Development

The bill increases membership of the subcabinet by adding the Secretary of Health and Mental Hygiene; Secretary of Labor, Licensing, and Regulation; and Director of the Maryland Energy Administration. The subcabinet is required to (1) work together to create, enhance, support, and revitalize sustainable communities; (2) upon application of a local jurisdiction, certify that the local jurisdiction has implemented regulatory streamlining or other development incentives in priority funding areas for the purpose of the rating system established under the sustainable communities tax credit program; and (3) in addition to designating sustainable communities, make recommendations to DBED on BRAC Zone designations, MDP on the SCTC program, and MDOT on TOD districts.

Under current law, the Secretary of Transportation may designate a TOD district in consultation with the Secretaries of Business and Economic Development, Housing and Community Development, Environment, and Planning; and (2) the local government or multi-county agency with land use and planning responsibility in the area. The bill replaces the first requirement and states the Secretary may designate a TOD district after considering a recommendation of the Smart Growth Subcabinet.

Maryland Department of Transportation

The bill contains intent language requiring MDOT to (1) consider sustainable communities as it considers annual revisions to the Consolidated Transportation Program; and (2) consult twice annually with the Smart Growth Subcabinet on how to work cooperatively to make mutual investments toward creating and supporting sustainable communities across the State. Subject to limitations specified under current law, MDOT may exercise all powers reasonably necessary to achieve sustainable community goals including the authority to: (1) adopt regulations to implement sustainable community objectives; (2) apply for and receive grants, gifts, payments, loans, advances, appropriations, property, and services from the federal and State government; and (3) enter into agreements and contract for (a) any studies, plans, demonstrations, or projects; (b) planning, engineering, and technical services; or (c) any purpose necessary or incidental to the performance of its duties and the exercise of its powers under sustainable communities.

Current Law:

Neighborhood Business Development Program

The purpose of the Neighborhood Business Development Program, commonly referred to as the Neighborhood BusinessWorks (NBW) Program, is to (1) help develop small businesses and microenterprises; (2) stimulate private-sector investment; and (3) invest in and stimulate local participation in small business and microenterprise revitalization projects.

With the concurrence of the Secretary of Housing and Community Development, a political subdivision may approve a designated neighborhood after considering (1) the availability, cost, and condition of business facilities; (2) the age and number of abandoned and substandard structures; (3) the relative income of residents; (4) the extent of unemployment in the area; (5) the need for small business, nonprofit, and microenterprise financing to upgrade social and economic conditions; (5) the development strategy of the political subdivision for the area; and (6) other standards DHCD considers relevant in regulations, including standards established for other State and federal programs. A designated neighborhood also includes areas located in a priority funding area and designated as a BRAC revitalization and incentive zone.

Community Legacy Program

The community legacy program under DHCD was established by Chapter 567 of 2001 to create a process and funding source for several types of revitalization projects. Community legacy projects include those that help create or preserve housing opportunities, support demolition of buildings or improvements to enhance land use, and develop public infrastructure (*e.g.*, parking, landscaping) related to a community legacy area. A community legacy area is the part of a priority funding area designated (1) by the Community Legacy Board; or (2) as a BRAC revitalization and incentive zone. The Community Legacy Program is jointly administered by the Community Legacy Board and DHCD. A community legacy plan or a community legacy project does not take effect until the Community Legacy Board has approved it. Under certain circumstances, the Secretary of Housing and Community Development may approve a community legacy project without approval of the board in the case of an emergency or when the project requires urgent approval. The advisory committee to the board makes recommendations concerning community legacy areas, community legacy plans, and community legacy projects and considers matters the board requests.

Heritage Structure Rehabilitation Tax Credit Program

The tax credit program terminates July 1, 2010. The section below discusses the main aspects and evolution of the program.

Background:

Heritage Structure Rehabilitation Credit

The Heritage tax credit program (Heritage tax credit) was part of a larger piece of legislation enacted in 1996 that was targeted towards heritage preservation and tourism. The Heritage tax credit replaced a subtraction modification for rehabilitating historic structures, and allowed taxpayers to claim a credit of up to 25% of expenditures. The new tax credit was much broader than the subtraction modification, and extended the credit to businesses that owned depreciable property. In addition, the new tax credit could be applied against the insurance premium tax, the financial institution franchise tax, or the public service company franchise tax. The Maryland Historic Trust was designated as the State entity responsible for administering the tax credit. In 2001, several changes were made to the Heritage tax credit including making a portion of the tax credit refundable.

Legislation enacted in 2002 session was the first of several significant legislative changes to the tax credit, primarily due to increasing concerns about the cost of the credit. Due to further legislative concerns about the cost of the credit, further substantial legislative changes were made in 2004. The commercial tax credit portion was shifted from a traditional tax credit program to a tax credit program that is subject to an annual appropriation in the State budget, with an aggregate limitation based on the final appropriation. The termination date was also extended to July 1, 2008. The value of the credit was again modified to 20% of the qualified rehabilitation expenditures expended in the rehabilitation of a certified historic structure. The maximum amount of credits earned for an individual rehabilitation project was set at a maximum of $50,000 for noncommercial projects; and the lesser of $3 million or the maximum amount stated on an initial credit certificate for commercial projects. MHT must award an initial credit certificate to each approved commercial rehabilitation plan based on the amount of estimated rehabilitation expenditures.

A reserve fund was established to offset future credits claimed for the rehabilitation of commercial properties. The General Assembly also specified that the total amount of initial credit certificates issued by MHT in each fiscal year cannot exceed the amount appropriated to the reserve fund. There was no aggregate cap or reserve fund, however, for residential tax credits. The Governor was required to appropriate to the reserve fund at least $20 million in fiscal 2006 and $30 million in fiscal 2007 and 2008. The Governor was not authorized to reduce an appropriation to the reserve fund that was approved by the General Assembly.

In 2007, the program’s termination date was extended through fiscal 2010 and no specific amount was required in the State budget. The maximum amount of total initial credit certificates issued in a fiscal year that could be allocated for projects located in one county or Baltimore City was increased from 50% to 75%.

During the 2009 session, the Administration introduced legislation that would have again significantly altered the Heritage Structure Rehabilitation Tax Credit program. As introduced, Senate Bill 258/House Bill 309 of 2009 would have converted the commercial tax credit program to a conventional tax credit program that would not be subject to an annual appropriation, eliminating the reserve fund used to offset future revenue losses from the commercial program, eliminating the geographic restriction on and competitive awarding of commercial credits, and making several other changes to the program. MHT would have been authorized to award a total of $100 million in commercial credits on a first-come, first-served basis to those qualifying applicants. A scaled down version of House Bill 309 retaining the commercial credit as a budgeted tax credit passed the House of Delegates, but failed in the Senate Budget and Taxation Committee.

Commercial Tax Credit Program

The Heritage tax credit for commercial properties has evolved into one of the State's largest economic development programs. Since 1997, a total of 447 completed commercial rehabilitations have earned credits totaling $238.5 million. In addition, 145 projects that are not yet completed will earn up to an additional $69.3 million in credits, bringing the estimated total funding to date to $307.8 million ($366.1 million adjusted for inflation). The commercial tax credit program is the largest business-related State income tax credit and one of the largest of all State income tax credits. Through tax year 2005, a total of $177 million in Heritage tax credits have been claimed (both residential and commercial projects). Since fiscal 2006, the commercial program has existed as a budgeted tax credit with an aggregate limit. From fiscal 2006 through 2010, MHT has awarded a total of $75.7 million in credits. This amount includes both final credits earned by completed projects and initial credit certificates issued to projects not yet completed.

Exhibit 1 lists the amount appropriated to the reserve fund in fiscal 2006 through 2010 and the actual amount MHT allocated in each year. The actual amount allocated may be different than the amount appropriated for several reasons, including Board of Public Works (BPW) funding reductions, expired credits, and "carry-over" credits that were appropriated but not allocated in the previous fiscal year. As part of overall cost containment actions, BPW reduced the amount appropriated to the reserve fund in fiscal 2008 through 2010 as well as reducing the reserve fund balance by $671,000 in each of fiscal 2008 and 2009. Slightly less than $10 million was not allocated in fiscal 2007 due to the geographic limitation in effect at the time and was instead allocated in fiscal 2008.

Exhibit 1
Heritage Structure Rehabilitation Tax Credit Reserve Fund
Commercial Projects
Fiscal 2006-2010

	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010
Appropriation	**20,000,000**	**30,000,000**	**15,000,000**	**14,700,000**	**7,000,000**
BPW Reductions			(300,000)	(4,700,000)	(2,000,000)
Net Appropriation	**20,000,000**	**30,000,000**	**14,700,000**	**10,000,000**	**5,000,000**
Carry Over	0	328,744	9,939,939	231,744	
Total Available	**20,000,000**	**30,328,744**	**24,639,939**	**10,231,744**	**5,000,000**
Reductions & Unallocated	(1,404,744)	(12,257,685)	(571,744)	(231,744)	
Net Allocated	**18,595,256**	**18,071,059**	**24,068,195**	**10,000,000**	**-**

Program Trends

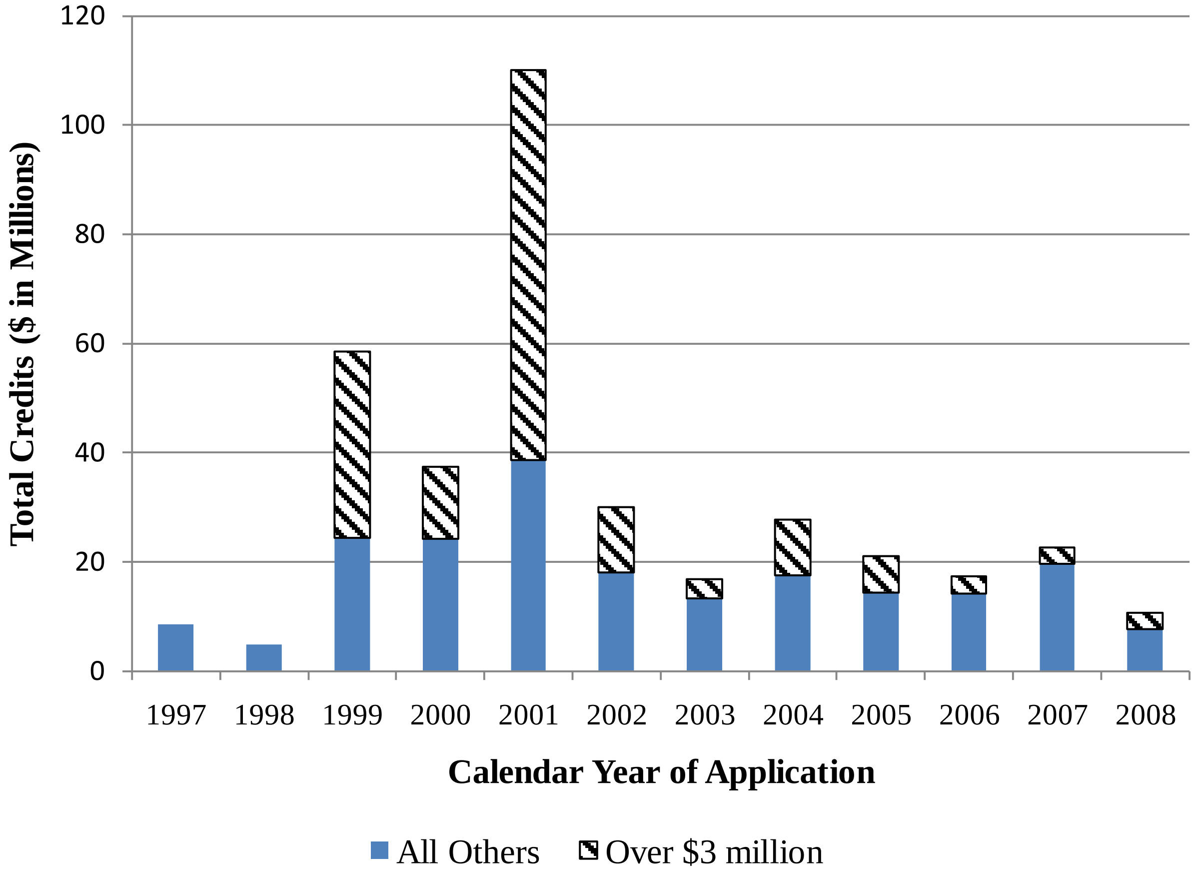
The program expanded significantly beginning in calendar 1999 and peaked in 2001 – projects beginning during these three years earned a total of $165.8 million in credits with over one-half of the total occurring during 2001. Legislation significantly curtailed the total amount of credits awarded to projects applying after 2002 – an average of $18.8 million in credits has been awarded in the last seven years of the program compared with $55.3 million in 1999 through 2001.

Exhibit 2 illustrates the total commercial credits awarded under the program according to the calendar year in which the project applied and separates the amount of credits earned in each year based on whether or not the credit earned a credit of $3 million or more.

Geographic Distribution

Exhibit 3 lists by county the number of projects, median credit earned, and total number of credits under the prior and current program.

Exhibit 2
Commercial Credits Earned by Size of Project and Date of Application
Calendar 1997-2008



Note: Amounts adjusted for inflation and expressed in 2008 dollars.

Source: Maryland Historical Trust, Department of Legislative Services

Exhibit 3
Commercial Tax Credit Projects Earned by County
Current and Prior Programs
1997-2009

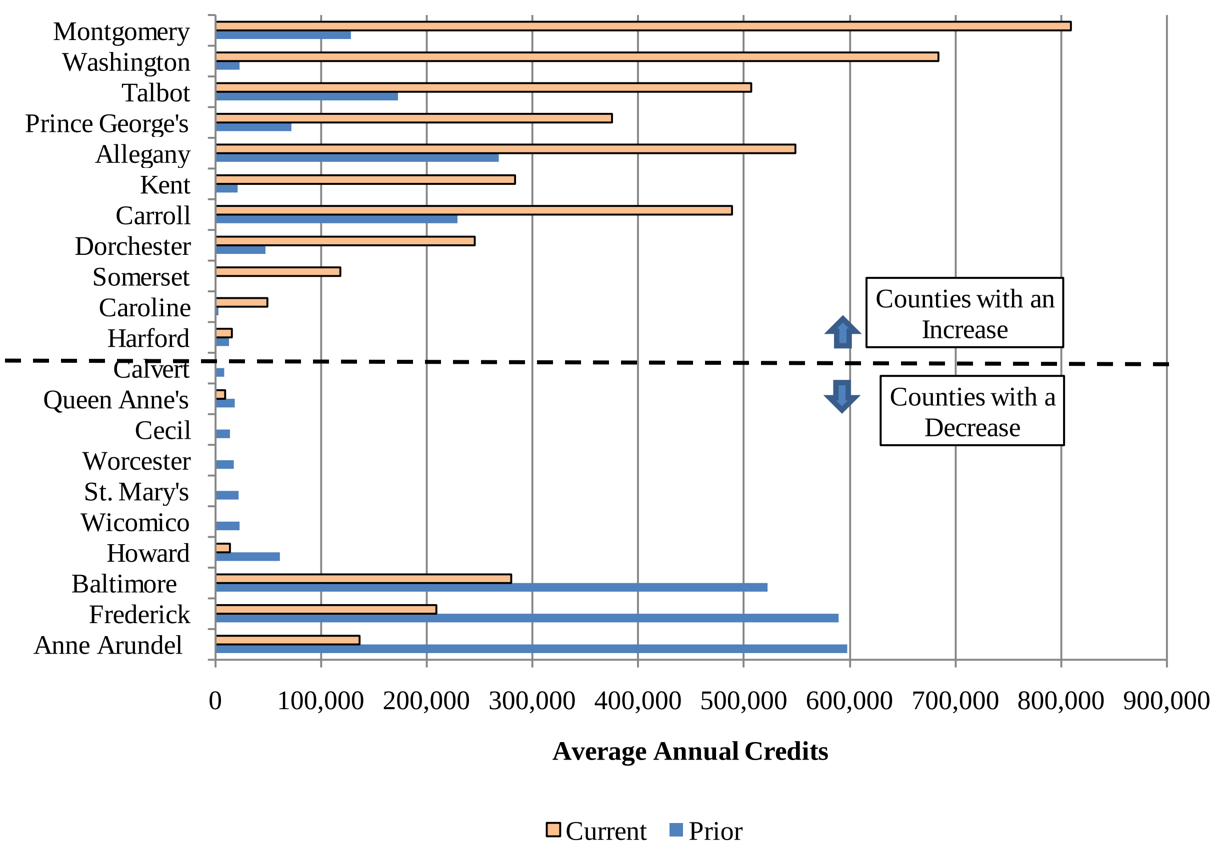
	Prior to Chapter 76 of 2004				Fiscal 2006 - 2009			
County	#	Median	Total	Percent Total	#	Median	Total	Percent Total
Allegany	15	$65,099	$2,147,010	0.9%	7	$140,000	$2,743,447	4.0%
Anne Arundel	17	57,260	4,778,139	2.0%	6	71,779	683,556	1.0%
Baltimore	15	48,774	4,177,740	1.7%	6	229,856	1,398,714	2.1%
Baltimore City	304	77,126	216,904,304	90.5%	84	92,500	44,185,176	64.9%
Calvert	1	63,852	63,852	0.0%	-	-	-	0.0%
Caroline	1	26,250	26,250	0.0%	3	41,600	247,599	0.4%
Carroll	8	43,592	1,829,320	0.8%	8	122,000	2,445,816	3.6%
Cecil	2	53,592	107,184	0.0%	-	-	-	0.0%
Charles	0	-	-	0.0%	-	-	-	0.0%
Dorchester	3	33,925	380,895	0.2%	6	175,000	1,225,326	1.8%
Frederick	16	79,669	4,719,472	2.0%	8	103,547	1,043,280	1.5%
Garrett	0	-	-	0.0%	-	-	-	0.0%
Harford	1	100,000	100,000	0.0%	1	80,000	80,000	0.1%
Howard	8	45,549	486,968	0.2%	1	70,000	70,000	0.1%
Kent	3	56,062	170,313	0.1%	5	280,000	1,416,965	2.1%
Montgomery	7	99,987	1,022,644	0.4%	4	511,382	4,047,812	5.9%
Prince George's	3	53,724	576,225	0.2%	4	322,918	1,875,836	2.8%
Queen Anne's	3	18,000	148,032	0.1%	1	44,888	44,888	0.1%
St. Mary's	2	86,307	172,614	0.1%	-	-	-	0.0%
Somerset	0	0	0	0.0%	3	160,000	589,641	0.9%
Talbot	10	55,000	1,378,460	0.6%	9	95,000	2,536,497	3.7%
Washington	4	43,039	183,580	0.1%	7	540,000	3,418,079	5.0%
Wicomico	3	75,000	184,497	0.1%	-	-	-	0.0%
Worcester	3	35,879	141,606	0.1%	-	-	-	0.0%
Total	**429**	**60,000**	**239,699,105**		**163**	**130,000**	**68,052,632**	

Source: Maryland Historical Trust, Department of Legislative Services

Baltimore City projects earned about 90% of all credits prior to Chapter 76 compared with about two-thirds under the current program. Overall, Baltimore City projects earned an average of $27.1 million in credits in the eight years under the prior program. Including calendar 2009 when no credits have been awarded, Baltimore City projects have earned an average of $8.8 million in credits under the current program – a decrease of about two-thirds.

In contrast to the experience of Baltimore City and the overall decrease in funding, the average amount of credits claimed by projects located in all other counties has increased from $2.8 million to $4.8 million. **Exhibit 4** illustrates the change in the average annual funding under the prior and current program for other counties that have received funding under the program. Counties located at the horizontal extremes of the graph experienced the largest absolute changes in annual funding while counties near the center experienced less substantial changes. For example, Montgomery County experienced the largest annual increase in funding ($681,700) compared with the largest annual decrease in Anne Arundel County ($460,600).

Exhibit 4
Change in Annual Funding under Current and Prior Program



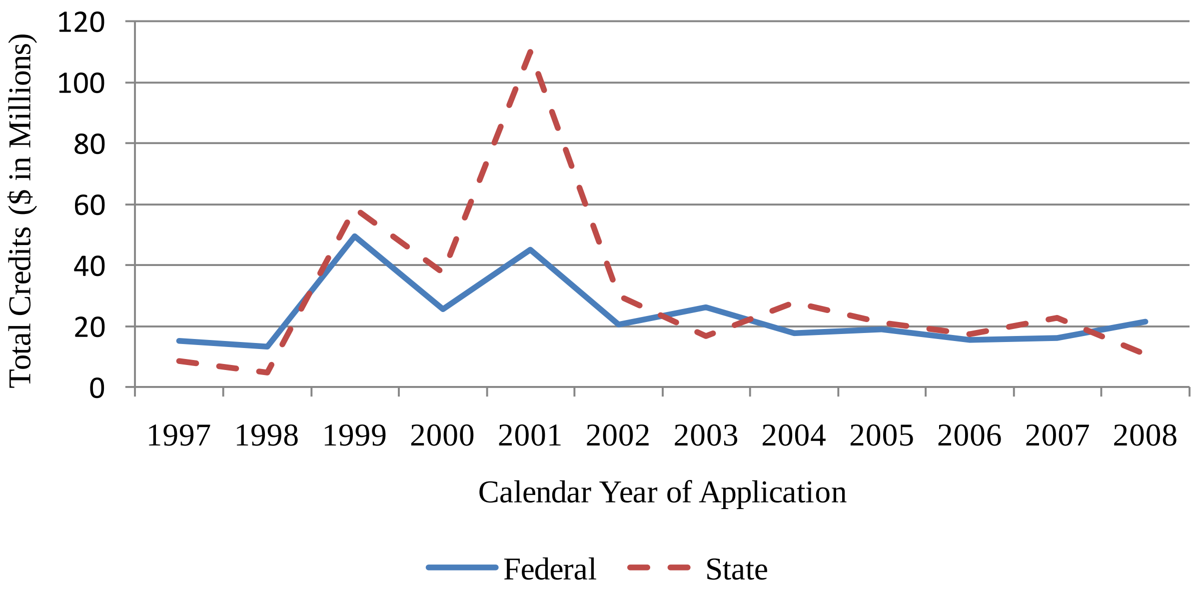
Source: Maryland Historical Trust, Department of Legislative Services

Federal Tax Credits in Maryland

Since 1997, a total of 501 rehabilitations located in the State have earned or will earn a total of $243.0 million in federal tax credits, based on $1.22 billion in rehabilitation expenditures. The median value of the federal credit earned by Maryland projects is $61,700, which translates to a rehabilitation project of $308,500. In an average year, 39 projects will claim about $20 million in federal credits. After reaching a peak of $45.2 million in 2001, rehabilitation activity has become less volatile – between $15.4 million and $17.8 million in credits have been earned in each of the last five years. Conversion of the State commercial tax credit program from an uncapped tax credit to a capped credit subject to an overall annual budget appropriation is likely one moderating influence.

Changes in the amount of federal credits in a year have often been similar to the change in State commercial credits claimed. **Exhibit 5** lists the number of federal and State commercial credits earned by date of application, adjusted for inflation and expressed in 2008 dollars.

Exhibit 5
Federal and State Commercial Credits Claimed by Application Date
Calendar 1997-2008

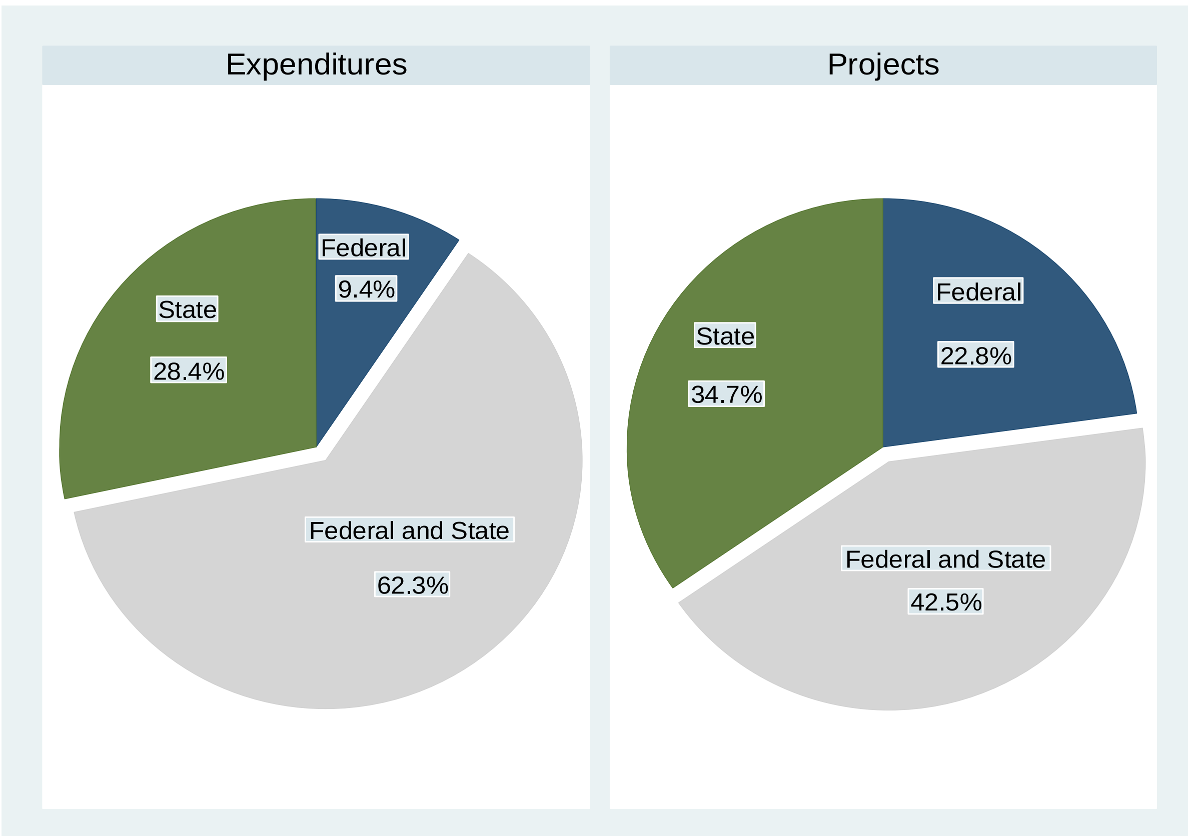


Note: Dollar amounts are adjusted for inflation and expressed in 2008 dollar values.

Source: Maryland Historical Trust, Department of Legislative Services

Exhibit 6 illustrates the estimated portion of all credit-claiming rehabilitation projects that earned the federal credit only, the State credit, and both credits as well as the percentage of all rehabilitation activity that each of these three categories composed. Since 1997, 23% of all projects claimed only the federal credit, 35% claimed only the State credit, and 42% claimed both credits. Larger-sized projects that claimed both credits accounted for 62% of all rehabilitation activity.

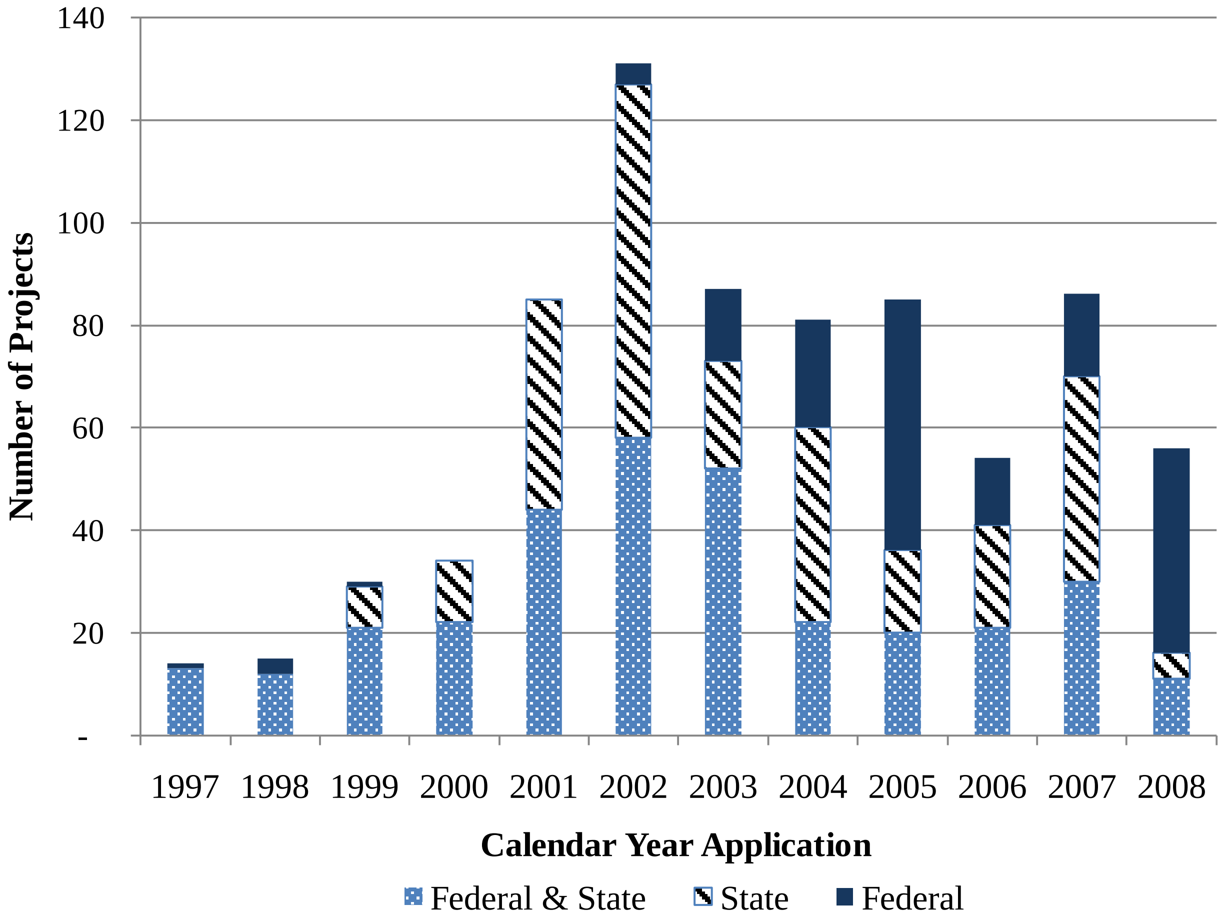
Exhibit 6
Percent of Rehabilitation Projects Earning Federal, State, or Both Credits
1997-2008



Source: Maryland Historical Trust, Department of Legislative Services

Exhibit 7 illustrates by calendar year of application the number of projects that claimed only the federal credit, both the federal and State commercial credit, and estimated number of projects that claimed only the State commercial credit. Since 2003, the distribution of project types has shifted towards federal only projects (34%) and away from combined (35%) and State-only projects (31%). In 2008 and 2009, State-only projects comprise less than 10% of all rehabilitations. Despite fluctuations in State funding and programmatic changes there have been a relatively constant number of rehabilitation projects in the State – an annual average of 83 projects with every year except two (2006 and 2008) reaching the 80-project threshold.

Exhibit 7
Number of Projects Earning Federal, State, or Both Credits
By Year of Application
1997-2008



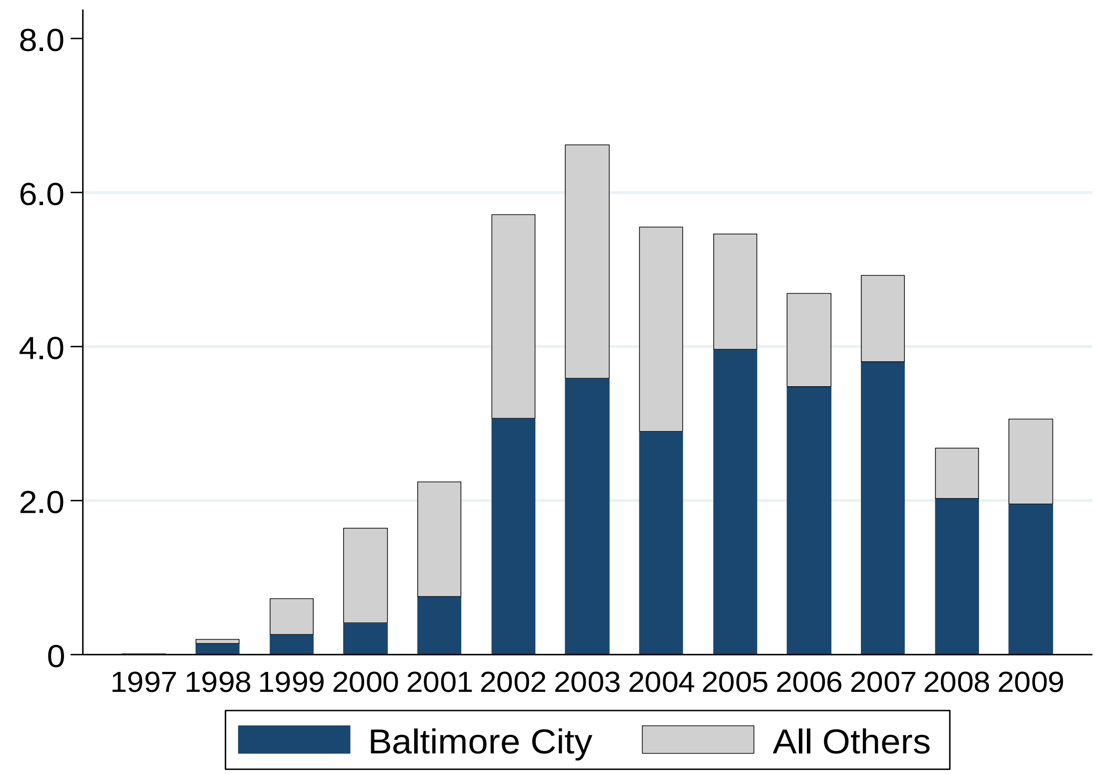
Residential Credit Program

Maryland is similar to most other states offering a historic rehabilitation tax credit – residential properties qualify for tax benefits in 25 of the 30 states that offer a credit. Although substantially smaller in scope than the commercial credit projects, about

2,500 residential projects have earned a total of $40.1 million in credits since the program's inception in 1997 ($43.5 million in current dollars after adjusting for inflation). A total of $194.7 million in residential rehabilitation expenditures have qualified under the program. Although the current maximum value of the credit is limited to $50,000, the median value of all credits earned since the program's inception is $7,210, which translates to rehabilitation project expenditures of about $35,200. Although the distribution of projects is skewed towards smaller-scale projects, a little more than 500 projects earning a credit of at least $25,000 comprise about one-fifth of all rehabilitations and claimed about two-thirds of all credits.

Exhibit 8 shows the amount of residential credits earned in Baltimore City and all other counties. After initial sluggish growth, the residential program experienced exponential growth through 2002 and remained relatively static through 2007 before the economic and housing market downturns stunted rehabilitations in 2008. Although the overall amount of credits has been relatively stable, credits claimed in counties other than Baltimore City peaked at $3.0 million in 2003 and have steadily decreased since, averaging a little less than $1 million annually in the last three years. About half of the decline for these counties is due to a large decrease in Anne Arundel County credits, with another 16% due to a decrease in Baltimore County. Nearly every remaining county also experienced substantial declines, except for Frederick and Cecil counties. In contrast, the credit decrease in 2008 and 2009 is driven largely by a decrease in Baltimore City projects – about $1.5 million lower in each of the last two years, compared with an annual average of $3.5 million from 2002 to 2007.

Exhibit 8
Total Residential Credits
1997-2009



Note: Figures adjusted for inflation and expressed in current dollars, through October 2009.

Source: Maryland Historical Trust, Department of Legislative Services

Neighborhood and Rehabilitation Project Characteristics

Legislative Services analyzed the assessed value of residential projects that received Part 3 approval during fiscal 2006. The median assessed value of all residences that earned a credit was $483,965 compared with an average assessed value of $326,000 for all State residences. Although roughly one-fifth (55 projects) of all projects have an assessed value of less than $300,000, only 7 projects or a little less than 2% had an assessed value of less than $200,000. Twenty-seven projects had an assessed value in excess of $1 million, representing about 10% of all projects and credits earned during the year.

Exhibit 9 lists project and credit distribution based on the median household income of the census tract in which the rehabilitation was located. Exhibit 9 splits the 200 Baltimore City census tracts into four equal parts – for example Quarter 1 represents the 50 census tracts (25% of total) with the lowest median household income and shows how many projects and credits were claimed in these census tracts. Quarters with more (less) than 25% of projects and credits have a high (low) utilization of the credit. Exhibit 9 also includes the median household income (not adjusted for inflation) in 1999 for each quarter.

Projects and credits are skewed towards higher-income census tracts. Quarter 1 contains only about 8% of all projects and 12% of all credits earned compared with the highest quarter, in which about 58% of all projects were located and a little more than two-thirds of all credits earned. Although both Quarter 2 and Quarter 3 had disproportionately fewer projects and credits claimed, almost twice the amount of credits were earned in Quarter 2 than Quarter 3, which had a similar number of projects as Quarter 1. About 41% of all projects and half of all credits were earned in 10 census tracts with the highest median household incomes in the city. About 11 projects on average were completed in each of the census tracts with the highest 5% of incomes compared with less than one in Quarter 1 through Quarter 3.

Exhibit 9
Baltimore City Residential Projects by Census Tract Median Income
Calendar 2005

Quarter	Median Income	Projects	Total Credits	Projects Per Census Tract	% Credits	% Projects
One (Lowest)	$18,292	17	484,980	0.34	12.2%	7.8%
Two	25,544	37	810,051	0.74	20.3%	17.1%
Three	32,614	19	385,009	0.38	9.7%	8.8%
Four (Highest)	43,045	144	2,306,221	2.88	57.9%	66.4%
Highest 5%	65,496	109	1,620,988	10.9	40.7%	50.2%
Total	**$30,078**	**217**	**3,986,261**	**1.85**		

Note: Median family income is for calendar 1999 and is not adjusted for inflation.

Source: Maryland Historical Trust, U.S. Census Bureau, Department of Legislative Services

Although the distribution of credits and projects was skewed towards higher-incomes, incomes in the city are significantly lower than the rest of the State. Median household income for the entire State was $57,868 – about double Baltimore City. In addition, significant variation exists within each quarter. In the eight census tracts in the lowest quarter with at least 1 project completion there was an average of 2.1 project completions per census tract – comparable to the average for the highest quarter. Compared with Baltimore City, projects in other counties during the same period are completed in census blocks with significantly higher median household incomes. Ninety-nine projects were completed in 64 different census blocks across the State. Almost 70% of all projects were completed in census blocks with median household incomes that were greater than the statewide average with about 10% of all project completions in census blocks with median household incomes in excess of $100,000.

Economic Impacts of the Credit

Several studies have examined the credit and have attempted to quantify its economic impacts. These studies have concluded that the credit has a large, positive impact on economic activity and job creation. A commonly referenced study concluded that each tax credit dollar is estimated to yield $8.53 in total economic activity during the construction period alone. A critical assumption of these studies is that none of the rehabilitation activity would have occurred in the absence of the credit or put another way, all of the economic activity related to historic rehabilitations was solely dependent on the existence of the State rehabilitation tax credit. Therefore, each dollar of credit induces $5 of rehabilitation activity which results in $8.54 in total State economic activity "during the construction period." However, the studies note that due to their challenging nature, most commercial projects would not be attempted without the equity provided by the combination of state and federal incentive activity." As noted previously, almost two-thirds of the commercial rehabilitation expenditures also claimed the federal credit as well.

In fiscal 2006, MHT could award no more than $20 million in credits during the fiscal year. A total of 36 projects received initial approval for $19.7 million in credits, representing $98.4 million in State credit-eligible rehabilitation activity. Due to the aggregate limitation and geographic restriction in place at the time, MHT denied $12 million in credits to 43 applicants located in Baltimore City. In the absence of aggregate and geographic limits, 79 projects would have been approved for $32 million in fiscal 2006. Total credit-qualifying rehabilitation activity would have increased by about $60 million to a total of $158 million.

Legislative Services examined fiscal 2006 applicants that did not receive funding in order to determine what impact, if any, denial of these applicants had on total commercial rehabilitation activity. A crucial assessment is whether or not these projects, in the absence of receiving the credit during fiscal 2006, proceeded with rehabilitation activity or abandoned the project due to a lack of State financing. In the absence of the credit, 70% of denied projects proceeded with rehabilitation activity – either because receipt of the federal credit was sufficient (about one-half of all denied projects) or because Baltimore City permitting activity suggests rehabilitation proceeded in the absence of any credit (about one-fifth). At a maximum, 25% of the denied projects (11 projects), and the resulting economic activity, could be viewed as totally dependent on the State tax credit, either because the project proceeded in subsequent years after receiving (only) the State tax credit or because the project did not receive either a federal or State credit and lacked evidence of permitting activity. Two projects (5%) could be classified as jointly dependent on the State and federal credit due to receipt of both credits. Based on the amount of rehabilitation activity reported by applicants who subsequently received either the federal or State rehabilitation credits, an additional $12 million in State rehabilitation credits would have been associated with an increase in commercial rehabilitation activity of between $20 to $25 million – a ratio of about 1.7 to 2.1 in additional rehabilitation expenditures for every additional State tax credit. This rough-order-of-magnitude estimate is substantially lower than the 5 to 1 ratio assumed by recent economic impact studies.

Historic rehabilitation activity also can qualify for numerous other federal, State, and local tax and economic incentives, further diluting the magnitude of the incentive of the State rehabilitation tax credit. Examples of other tax credits include the federal low-income housing and new markets tax credit, State enterprise zone and brownfields credits, and local historic rehabilitation property tax credits. A recent U.S. Government Accounting Office (GAO) report highlights the significant overlap among federal, State, and local incentives among economic projects. In analyzing the new markets tax credit, GAO found that one-half of the recipients packaged the federal credit with another state, federal, or local incentive and among those receiving multiple incentives, 30% also received the federal rehabilitation credit and 35% received a State or local tax incentive.

Legislative Services examined State Department of Assessments and Taxation data on 19 commercial projects that have received final certification and earned a credit of at least $3 million. One-third of the rehabilitations that were identified as claiming Enterprise Zone property tax credits are claiming the credit on average eight years since Heritage tax credit application and four years after completion of the historic rehabilitation. In tax year 2009, the State will reimburse Baltimore City $2.6 million for these projects.

State Revenues: The bill authorizes MHT to award a total of $50 million in commercial credits beginning October 1, 2010, and extends the residential program, which terminates July 1, 2010, under current law. As a result, general fund revenues will decrease by

$6.5 million in fiscal 2012. **Exhibit 10** details the impact of the bill on revenues in fiscal 2011 through 2017.

Revenue losses could be significantly higher than estimated in the early years of the program to the extent that a higher number of commercial rehabilitation projects are completed earlier than estimated. This forecast is based on the existing history of the program and extending the commercial program to other types of rehabilitations may impact the timing of revenue losses. Legislative Services advises that converting the commercial tax credit program to a conventional tax credit program without a reserve fund will significantly increase the uncertainty over the timing of program's fiscal impact. Annual revenue losses could be substantially higher than estimated in each fiscal year. The timing issue of when revenues losses occur does not, however, alter the $50 million total cost of extending the commercial tax credit program.

Exhibit 10
Impact on State Finances

	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017
Revenues							
Residential Credits	$0	$3,719,100	$8,143,400	$5,252,700	$4,886,100	$0	$0
Commercial Credits	0	2,778,200	6,305,200	15,769,500	13,624,000	9,782,000	1,741,200
Total Credits (GF)	0	6,497,300	`14,448,600	21,022,200	18,510,100	9,782,000	1,741,200
MHT							
Fee Revenues (SF)	261,400	266,000	279,100	292,800	0	0	0
Administrative Expenses	261,400	266,000	279,100	292,800	0	0	0

The Department of Budget and Management advises that the Governor's proposed budget includes a reduction of revenues in fiscal 2012 through 2016 due to extension of the credit. Revenues are reduced by $5.0 million in fiscal 2012, $13.0 million in fiscal 2013, $14.5 million in fiscal 2014, $10.5 million in fiscal 2015, and by $7.0 million in fiscal 2016.

Any unencumbered funds in the Heritage Structure Rehabilitation Tax Credit Reserve Fund revert to the general fund on June 30, 2014. Under current law, money in the reserve fund is used to offset general fund losses resulting from completed projects. Transferring the money back to the reserve fund will not materially affect State finances.

Residential Rehabilitation Credits

There is no limitation on the amount of credits that can be earned in a year by residential projects. Based on the correlation of residential credits claimed, State home sales, total residential improvement expenditures, and the forecasts for these other variables; Legislative Services estimates that approximately $3.7 million in credits will be claimed in fiscal 2012 as shown in Exhibit 10. The bill also expands eligibility of the residential credits to nonhistoric residences located in certain areas of priority funding areas. As a preliminary estimate, it is estimated that allowing residences in designated sustainable communities in fiscal 2012 to be eligible for the credit will double the cost of the credit in fiscal 2013. The actual revenue loss could be significantly more. MDP is preparing an estimate of how many additional housing units could qualify as a result of the expansion of the bill.

The bill is effective October 1, 2010. It is assumed that this is the earliest date MHT will process applications and no projects will be completed and certified within calendar 2010. To the extent projects are completed in calendar 2010, revenue losses will occur in fiscal 2011.

MHT Administrative Fees

The bill extends MHT's authority to charge a fee, not to exceed 2% of the estimated value of credits issued, that is sufficient to pay the cost of administering the State and federal historic tax credit. The bill creates an administration fund that will receive certification fees and can be used for federal and State tax credit administrative fees. **Exhibit 10** lists the estimated amount of fee revenue deposited in the fund in each fiscal year based on the estimated amount of commercial and residential applications in each year.

State Expenditures: Under current law, the tax credit program operates through fiscal 2010. Special fund expenditures will increase beginning in fiscal 2011 at MHT as a result of extending the tax credit program. Exhibit 10 lists the estimated cost of administering the program in fiscal 2011 through 2014.

The fiscal 2011 allowance includes $5.0 million in funding for the Heritage Rehabilitation Tax Credit Reserve Fund for commercial projects. The budget bill contains language that deletes the entire appropriation contingent upon enactment of legislation reauthorizing the program as a nonbudgeted tax credit.

Additional Information

Prior Introductions: None.

Cross File: HB 475 (The Speaker, *et al.*) (By Request - Administration) – Ways and Means and Environmental Matters.

Information Source(s): Department of Budget and Management, Maryland Department of Planning, Maryland Historic Trust, Department of Legislative Services

Fiscal Note History: First Reader - February 16, 2010
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ANALYSIS OF ECONOMIC IMPACT ON SMALL BUSINESSES

TITLE OF BILL: Smart, Green, and Growing - The Sustainable Communities Act of 2010

BILL NUMBER: SB 285

PREPARED BY: Michael K. Day

PART A. ECONOMIC IMPACT RATING

This agency estimates that the proposed bill:

____ WILL HAVE MINIMAL OR NO ECONOMIC IMPACT ON MARYLAND SMALL BUSINESS

OR

__X__ WILL HAVE MEANINGFUL ECONOMIC IMPACT ON MARYLAND SMALL BUSINESSES

PART B. ECONOMIC IMPACT ANALYSIS

As reported in an independent study of the Maryland Heritage Structure Rehabilitation Tax Credit Program commissioned by the Abell Foundation and released in draft form on February 3, 2009 by the accounting firm of Lipman, Frizzell & Mitchell, "over the 12 years, completed commercial projects have generated a total economic impact on the Maryland economy of more than $1.74 billion (in 2009 dollars) in total economic activity, employing an estimated 15,120 persons earning $673.1 million (in 2009 dollars). Construction labor on the job-sites totaled an estimated 9,248 workers earning $443.4 million (in 2009 dollars) – over three-fifths of the total economic impact." The majority of these jobs went to workers who were employed by small businesses located in the vicinity of the tax credit assisted projects. Regarding fiscal impact, the draft report states that "during their construction periods alone, the 407 projects [commercial projects completed during the first 12 years] generated an estimated $83.7 million (in 2009 dollars) in State and local taxes – effectively paying down more than one-third of the State's total $213.9 million tax credit investment. The greatest return on the State's investment, however, comes from the long-term increase in employment and property taxes at the historic properties and their neighbors in perpetuity." For the same 12-year period, the draft report states that "residential projects have generated a total economic impact on the Maryland economy of more than $354.9 million (in 2009 dollars) in total economic activity, employing an estimated 3,343 persons earning $88.5 million (in 2009 dollars). Construction labor and on the job-sites totaled an estimated 1,606 workers earning $38.9 million (in 2009 dollars) – almost half of the total economic impact." The draft report also states that "during their construction periods alone, the 2,351 projects generated an estimated $23.5 million (in 2009 dollars) in State and local taxes – effectively paying down more than one-third of the State's total $41.6 million tax credit investment. The greatest return, however, comes from the long-term increase in property taxes for the historic properties and their neighbors in perpetuity." Again, the majority of these jobs went to workers who were employed by small businesses located in the vicinity of the tax credit assisted projects. SB 285 will expand opportunities for small businesses, effecting construction contractors in all trades, wholesale and retail building material suppliers as well as small architectural and engineering businesses.