Department of Legislative Services

Maryland General Assembly
2016 Session

FISCAL AND POLICY NOTE
Third Reader - Revised

Senate Bill 455 (Senator McFadden)
Budget and Taxation Rules and Executive Nominations

State Education Aid - Real Property Valuation - Tax Increment Financing

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This bill authorizes grants, for fiscal 2018 and 2019, to counties that establish a tax increment financing (TIF) development district after May 1, 2016, and qualify for State disparity grant funding. For fiscal 2018 and 2019, using net taxable income (NTI) based on tax returns filed on or before November 1, State aid (excluding NTI grants) must be calculated once using the assessed valuation of real property as defined by current law and again using that same valuation as reduced by the calculated tax increment due to the TIF district (as described below) for each eligible county. If the amount of State aid calculated as reduced by the tax increment is *greater* than the amount of State aid calculated without excluding the tax increment, the difference is provided as a grant to the county board of education. The bill also states legislative intent that the adequacy of the education funding study consider the impact of economic development incentives in low-wealth counties on State education aid and make recommendations on specified topics.

The bill takes effect June 1, 2016, applies to the calculation of State education aid payments beginning with fiscal 2018, and terminates June 30, 2019.

Fiscal Summary

State Effect: The bill may increase State education aid, potentially significantly, depending on the amount of any tax increment in a TIF district that is excluded from a county's assessable base in a given year in counties that qualify for State disparity grant funding. However, it is unlikely that any significant tax increments will be realized during the effective period of the bill. **This bill establishes a mandated appropriation in FY 2018 and 2019.** No effect on revenues.

Local Effect: Some local school systems may receive more State education aid in FY 2018 and 2019 than under current law depending on the number of TIF districts and the value of any tax increments in these districts that is excluded from the assessable base in counties that qualify for State disparity grant funding.

Small Business Effect: None.

Analysis

Bill Summary: The State Department of Assessments and Taxation (SDAT) must (1) certify the original amount of assessable base for real property that is located in an eligible TIF development district as of January 1 of the year preceding the year in which the ordinance or resolution establishing the TIF development district takes effect and (2) annually certify the amount of assessable base for real property that is located in the eligible TIF development district as of July 1 of the first completed fiscal year before the school year for which the calculation of the grant is made. For TIF development district real property, the tax increment is the difference between the annually certified assessable base amount and the original certified assessable base amount.

The bill expresses the intent of the General Assembly that the final recommendations of the study of the adequacy of education funding being conducted as required by Chapter 288 of 2002 (The Bridge to Excellence in Public Schools Act), as amended by Chapter 397 of 2011, and any commission that may be established to make recommendations on the adequacy study, shall consider the impact of economic development incentives in low-wealth jurisdictions on State education aid, including the exclusion provided under § 5-202(l) of the Education Article as enacted by this Act.

Specifically, the adequacy study and any commission must make recommendations on (1) whether the assessed value of TIF districts should be excluded from the calculation of wealth for State education aid purposes and, if so, any limits on the exclusions that should be considered and (2) the continuation of the hold harmless grants established by the bill.

Current Law: The majority of State education aid is distributed through formulas that allocate funding to the 24 local school systems inverse to local wealth per pupil. For the purpose of calculating State aid to public schools, wealth is the sum of 100% of the assessed value of the operating real property of public utilities, 40% of all other real property assessed value, 50% of personal property assessed value, and 100% of net taxable income.

Tax Increment Financing

All counties and municipalities are authorized to utilize tax increment financing under Title 12, Subtitle 2 of the Economic Development Article (the Tax Increment Financing Act). In Baltimore City, the authority to use tax increment financing is provided in the city charter. Counties and municipalities (including Baltimore City) may issue bonds to finance the development of an industrial, commercial, or residential area. Generally, the bond proceeds may only be used (1) to buy, lease, condemn, or otherwise acquire property or an interest in property in the development district, a Regional Institution Strategic Enterprise (RISE) zone, or a sustainable community; or needed for a right-of-way or other easement to or from the development district, a RISE zone, or a sustainable community; (2) for site removal; (3) for surveys and studies; (4) to relocate businesses or residents; (5) to install utilities, construct parks and playgrounds, and for other needed improvements including roads to, from, or in the development district; parking; and lighting; (6) to construct or rehabilitate buildings for a governmental purpose or use; (7) for reserves or capitalized interest; (8) for necessary costs to issue bonds; and (9) to pay the principal of and interest on loans, advances, or indebtedness that a political subdivision incurs for a specified purpose.

Bonds issued for use in a sustainable community or a RISE zone have different use criteria.

The "original base" for a TIF district means the assessable base of the district:

- as of January 1 of the year preceding the effective date of the resolution creating the district; or
- if applicable, the original base for a brownfields site as determined by resolution of the political subdivision.

Disparity Grant

The disparity grant program provides State aid to low-wealth jurisdictions for county government purposes. The program reflects the State's policy to improve fiscal equity among jurisdictions by making less affluent jurisdictions less dependent on their own tax base to fund public services. Specifically, disparity grants address the differences in the abilities of counties to raise revenues from the local income tax, which for most counties is one of the larger revenue sources. Through fiscal 2010, counties with income tax rates of 2.4% or higher with per capita local income tax revenues less than 75.0% of the State's average (assuming a 2.54% statewide county income tax rate) received a grant equal to the dollar amount necessary to raise the county's per capita income tax revenues to 75.0% of the State average. Chapter 487 of 2009 included a provision, beginning in fiscal 2011, that capped each county's funding under the program at the fiscal 2010 level.

Chapter 425 of 2013 modified the formula to add a minimum grant amount based on local tax effort of eligible counties and raised from 2.4% to 2.6% the local income tax rate required to be eligible to receive a grant. Beginning in fiscal 2014, the fiscal 2010 amount cap continues to apply, but an eligible county or Baltimore City may receive a minimum amount (that can exceed the fiscal 2010 cap) based on local tax effort. The minimum amounts are (1) 20.0% of the uncapped grant amount if the local income tax rate is at least 2.8% but less than 3.0%; (2) 40.0% of the uncapped grant if the rate is at least 3.0% but less than 3.2%; or (3) 60.0% of the uncapped grant if the rate is at 3.2%.

Adequacy Study

Chapter 288 of 2002, the Bridge to Excellence in Public Schools Act, required the Maryland State Department of Education, in consultation with the Department of Budget and Management and the Department of Legislative Services (DLS), to contract with a consultant to conduct a follow-up study of the adequacy of education funding in the State approximately 10 years after its enactment.

After legislation in 2011 and 2012 delayed the beginning of the study and required additional reports to be included in the study, work on the adequacy study began in June 2014, when a contract was awarded to Augenblick, Palaich, and Associates and its team of researchers that includes Picus, Odden and Associates and the Maryland Equity Project. The final report must be submitted to the Governor and General Assembly by December 1, 2016.

Background:

Tax Increment Financing in Maryland

Tax increment financing is a public financing method that uses future gains in tax revenues to finance current improvements. The increase in the property tax revenue generated by new commercial development in a specific area, the TIF district, pays for bonds issued to finance site improvements, infrastructure, and other project costs located on public property. In a TIF district, the local government "freezes" the existing property tax base and uses the property tax revenue from this base as it would normally use such funds. The difference between the current tax base and the frozen base in each future year is termed the incremental valuation. The local government apportions the property tax revenue on the incremental valuation to a special account for certain purposes including to pay debt service on the bonds and to potentially pay for additional public expenditures in the TIF district. The TIF district ceases to exist upon the retirement of the bonds, and after that time, all property tax revenue may be appropriated by normal means.

According to SDAT, seven jurisdictions – Baltimore City and Anne Arundel, Baltimore, Harford, Howard, Prince George's, and Wicomico counties – have seen an increase in the assessable base in fiscal 2016 over the year the TIF districts were established. **Exhibit 1** shows the number of TIF districts by jurisdiction and the estimated tax increment for the seven jurisdictions with TIF districts as of March 2015.

Exhibit 1
TIF Districts and Combined Values by Jurisdiction

County	Number of Districts	Combined Value ($ in Millions)
Allegany	0	
Anne Arundel	7	$4,708.3
Baltimore City	9	475.0
Baltimore	1	30.8
Calvert	0	
Caroline	0	
Carroll	0	
Cecil	0	
Charles	0	
Dorchester	0	
Frederick	0	
Garrett	0	
Harford	1	59.5
Howard	1	6.3
Kent	0	
Montgomery	0	
Prince George's	7	1,441.9
Queen Anne's	0	
St. Mary's	0	
Somerset	0	
Talbot	0	
Washington	0	
Wicomico	2	8.9
Worcester	0	
Total	**28**	**$6,730.6**

Source: State Department of Assessments and Taxation; Baltimore City; Anne Arundel and Prince George's counties; Department of Legislative Services

Progress of Adequacy Study

The primary study on adequacy of education funding is on target to be completed by November 2016, using three different methodologies: evidence-based; professional judgment; and successful schools. All of the completed reports and

APA Consulting's presentations to the Adequacy Study Stakeholder Advisory Group can be found at http://marylandpublicschools.org/adequacystudy/. Also, information on progress of the adequacy study can be found in the *Issue Papers, 2016 Legislative Session* publication.

In looking at local wealth, in one of several final reports that have been submitted thus far, the consultants considered how Maryland combines property values and net taxable income to determine local fiscal capacity. Maryland's three-year reappraisal process for assessing property wealth was found to be reasonable. The study recommended that, similar to 10 other states, a portion of the assessed value effectively lost through tax increment financing should be subtracted from the calculation of local wealth so districts' equalization funding is more closely related to what is actually raised through property taxes. The study also recommended that Maryland consider Ohio's approach, which excludes a portion of the incremental value of TIFs from the local assessable property base for education aid purposes for up to 10 years.

Disparity Grant Counties

For fiscal 2017, Baltimore City and nine counties (Allegany, Caroline, Cecil, Dorchester, Garrett, Prince George's, Somerset, Washington, and Wicomico) qualify for disparity grants. The fiscal 2017 State budget includes $136.7 million for disparity grants.

State Expenditures: The bill may have a significant effect on State education aid depending on the amount of any tax increment in a TIF district that is excluded from a county's assessable base in a given year. Generally, when some amount of the assessable base is excluded from a more affluent county's total assessable base, with regards to the funding formula, overall State aid will decrease, and when some amount of the assessable base is excluded from a less affluent county's assessable base, overall State aid will increase.

The bill applies, for a three-year period, to future TIF districts established after May 1, 2016. The effect of the bill is difficult to project and will depend on several factors such as the number of TIF districts that are created, where these districts are created, and the tax increment resulting from these districts during the effective period of the bill. Since Baltimore City and nine counties (Allegany, Caroline, Cecil, Dorchester, Garrett, Prince George's, Somerset, Washington, and Wicomico) currently qualify for disparity grants, it is presumed that these jurisdictions are among those likely to qualify for grants under the bill.

DLS is aware of three proposed development projects involving TIF funding in Baltimore City. Expansion of the University of Maryland's BioPark in West Baltimore will include $17.5 million in TIF funding. Poppleton redevelopment, which includes plans to build about 1,600 residences, commercial space, a park, and a school in West Baltimore, will receive $58.3 million in TIF funding. Finally, $535.0 million in TIF funding has been requested from Baltimore City for the new Under Armour headquarters in Port Covington. In addition, reports indicate that the bid to bring the Federal Bureau of Investigation headquarters to Prince George's County may involve approximately $160 million in TIF funding.

However, regardless of the eventual estimated full value of the TIF projects, including those cited above, only the amount of increment that is generated within the effective period of the bill will impact State aid funding; TIF projects often last for two or three decades, with the increment increasing over time. Thus, it is unlikely that the bill will result in a significant, if any, increase in State education aid in fiscal 2018 and 2019.

Local Fiscal Effect: The bill may increase the total amount of State education aid distributed to counties that qualify for disparity grant funding. As noted above, the effect will depend on several factors such as the number of TIF districts that are created, where these districts are created, and the tax increment resulting from the creation of these districts; a significant increase in education aid is unlikely before the bill terminates after fiscal 2019.

Additional Information

Prior Introductions: None.

Cross File: HB 285 (Delegate McIntosh, *et al.*) - Appropriations.

Information Source(s): *The Baltimore Sun*; *Washington Business Journal*; Baltimore City; Anne Arundel, Harford, and Prince George's counties; Maryland State Department of Education; Department of Budget and Management; State Department of Assessments and Taxation; Department of Legislative Services

Fiscal Note History: First Reader - February 8, 2016
kb/rhh Revised - Senate Third Reader - April 8, 2016

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