WHEDA®

Property Tax Exemption Issue
Raised by
Columbus Park Housing Corporation v. City of Kenosha

Potential Effects for
Wisconsin Housing and Economic Development Multifamily Portfolio
And Preservation Initiatives

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Executive Summary

- **The results of the analysis on existing WHEDA portfolio indicated that immediate cash need for WHEDA financed affordable housing projects is approximately $3 million ($9 million if assessors reach back two years).**
- **It was necessary for WHEDA to add fifteen properties to our own targeted Saving our Stock (SOS) program – an increase of $1.5 million in immediate need (again $4.5 million if assessors reach back) – as a result of this court ruling.**
- **Future preservation efforts rely on not-for-profit participation. One of the ways the not-for-profits are able to reduce expenses to hold property in perpetuity is by benefit of a property tax reduction and/or exemption, freeing up additional income to reinvest in the property. That "incentive" will be eliminated making it more difficult to address the pressing need of preserving the existing affordable housing stock, both federally subsidized and expiring through the low-income housing tax credit "The Y15 program".**

The Challenge

On November 19, 2003 the Wisconsin Supreme Court filed its decision in the above referenced case. At the heart of the matter is language contained in the introductory Section 70.11, *Wisconsin Statutes* (Lessee Identity Condition) regarding property tax exemption that reads:

> *Leasing a part of the property described in this section does not render it taxable if the. . .lessee would be exempt from taxation under this chapter it if owned the property.*

The application of this language on WHEDA's multifamily portfolio means that our "benevolent" owners (usually defined internally as not-for-profits) can own and rent their apartment developments, but if the residents would not be exempt under the Statute if they owned the property, it is ineligible for property tax exemption. In practice this clause had not been applied to residential property.

Potential Impact – Current Portfolio

A cursory review of the WHEDA financed, multifamily portfolio indicates that 145 developments, containing over 6,600 units are currently owned by not-for-profit entities or Public Housing Authorities. These entities were either currently exempt from property taxes or had negotiated a payment in lieu of taxes (PILOT) within their municipality under the existing Statute. An analysis was completed to determine the potential effect on the financial stability of these developments should full taxation be implemented.

Several assumptions were utilized:

1. It appears property of Public Housing Authorities is exempt from taxation under Section 66.1202(22), Wis. Stats., though it is not entirely clear. We assumed these properties would remain exempt or maintain any PILOT they may have negotiated so no dollar need was identified, yet the units are represented in the totals on the attached map. If the PHAs are removed from the total, 123 developments containing over 5,400 units would be affected.
2. Since assessments are unavailable for the remaining portfolio, an average tax per unit, by county was calculated from WHEDA's for-profit portfolio. This average was applied to each affected development based on number of units so an estimated tax could be assumed.
3. The assumed tax was deducted from the property's most currently reported net operating income (NOI) and debt service coverage (DCR) was recalculated. To predict the dollar impact against the portfolio, the increase in tax used:
   - If current DCR was >1.0 and deduction of tax resulted in DCR still >1.0, the increase was included in full.
   - If current DCR was >1.0 and deduction of tax resulted in DCR <1.0, the increase was reduced just to get the property back to breakeven.
   - If current DCR was <1.0 and deduction of tax resulted in further reduction, the increase was included in full.
4. Under Section 70.44 of the Statutes, it appears that the assessor may also be able to add an assessment for property omitted from the tax rolls for two previous years.

The results of the analysis indicated that immediate cash need for the developments is approximately $3 million ($9 million if assessors reach back two years). It should be noted, that this estimate is based on "point in time" as of the reported 2002 financial condition of the developments. This estimation would be expected to increase in ensuing years. A map of the location of the affected developments is attached.

Potential Impact – Preservation Initiative

In addition, staff revisited the financial stress tests - designed as a result of the rent comparability rules imposed by HUD - conducted on WHEDA's project-based Section 8 portfolio. **Under the *Wisconsin SOS* program being developed, we had proposed a $10 million WHEDA commitment for the preservation of subsidized housing throughout the state.** Our original analysis indicated that approximately half of that amount would be needed to address stress within our own portfolio, the remaining funds to be used to spur preservation throughout the state. **It was necessary for WHEDA to add fifteen properties to our own targeted preservation list – an increase of $1.5 million in immediate need (again $4.5 million if assessors reach back) – as a result of this court ruling.**

The Governor also recently announced the formation of an all-inclusive preservation task force to address the pressing need of preserving the existing housing stock, both federally subsidized and expiring through the low-income housing tax credit program. HUD and the IRS, through regulation and application have shown preference to not-for-profit ownership. **The basis for this preference are three fold; 1) the housing is thought to be held in perpetuity by the benevolence of the ownership entity, 2) the not-for-profit owners typically are located within the market that the property is situated and can address changing market conditions more readily, and, 3) it is believed that the not-for-profit owners can operate the properties less expensively. However, one of the ways the not-for-profits were able to reduce expenses was by benefit of a property tax reduction and/or exemption, freeing up additional income to reinvest in the property. That "incentive" will be eliminated.**