HAGOPIAN MEMO NO. 5

TO: MEMBERS, SPECIAL COMMITTEE ON TAX EXEMPTIONS, Wisconsin Legislative Council Special Committee On Tax Exemptions For Residential Property (*Columbus Park,* 2003 WI 143), 2003 WI Act 195, 2003 SB 512

FROM: GREGG C. HAGOPIAN, Assistant City Attorney

DATE: January 14, 2005, Meeting No. 4

RE: **Legis. Council Drafts 0086/1 and 0090/1**

A. PROPOSALS.

1. **Hagopian Memo 4 Suggestions.** Creates new subcategories within 70.11(4). Would impose the homestead credit limit ($24,500) for benevolent residential housing, or, if law for benevolent associations stays unchanged, then would mandate a PILOT and appraisals (every 5 years). PILOT would be City rate times assessed value. And, assessor would have benefit of appraisals to help with assessment.

2. **Legis. Council Drafts.**

   a. **0086/1**. Creates new subcategories within 70.11(4). Adopts IRP 96-32 for low-income housing. Would mandate a payment for municipal services from 70.11(4)(c)9 category (residential housing of benevolent assn. that is not within subcategories 1-8). Requires 70.11(4)(c)9 category to file annual exemption requests under new 70.1103 and to provide appraisals.

   b. **0090/1**. Creates new subcategories within 70.11(4). Adopts IRP 96-32 for low-income housing. Does not have the subcategory (4)(c)9 category like 0086/1.

B. REACTIONS TO WHEDA PROPOSALS.

1. Good to break up 70.11(4) categories.

2. Good to try to define, refine, and limit the sub 4 realm of exemptions.

3. Neither the Committee nor the Legislature should embrace or adopt **IRP 96-32**. **Copy attached.** Has the Committee read 96-32? Will assessors be able to apply it?

    a. 96-32 does not set a clear income limit.

    b. While 96-32 does have a safeharbor (see § B.9. below; at least 75% units occupied by "low-income" and either at least 20% occupied by "very low income" or 40% occupied by those who do not exceed 120% of area's "very low income" limit. Up to 25% of units may be provided at market rates to persons with incomes in excess of "low-income" limit), 96-32 goes much further.

        - Very low income is 50% of area median income.
        - Low income is 80% of area median income.
        - But, per IRP 96-32, above percentages can be adjusted by HUD to reflect economic differences (such as high housing costs) in each area. And, income limits are tailored to relect different family sizes.
        - And, a resident's income can increase above the limits so long as the resident does not exceed 140% of the applicable income limit. And, even if the resident's income limit does increase over the 140% applicable income limit, that is OK if the organization rents "the next comparable non-qualifying unit to someone under the income limits."
        - And, an organization may meet the 96-32 requirements by providing "assistance to the aged or physically handicapped who are not poor" if the organization meets requirements in other specified IRS revenue rulings including 72124, 79-18, 79-19. This brings us back to financial prescreening to only those who can afford admittance get admitted. And, an organization with a mix of elderly or handicapped residents and low-income residents may meet 96-32 requirements under a "facts and circumstances" exception.

c. Transitional period of up to 1 year (or longer if project operates under a govt program with longer period) is allowed for projects under construction or rehab.

d. Reference is made to unspecified govt programs for rent restrictions or govt imposed mortgage limits.

e. If a project consists of multiple buildings, then some buildings could be at market rates while others are not – so long as the buildings "share the same grounds." But, this "shared ground" requirement does not apply to organizations that provide individual homes or individual apartment units at scattered sites to families with incomes at or below 80% of area median income.

f. 96-32's "facts and circumstances" provisions allow an organization to satisfy 96-32 even if the safe-harbor requirements (income limits) are not met. These facts and circumstances include as examples operation through a community board of directors, some relationship with some other 501(c)3 corp active in low-income housing, provision of "additional" but unspecified "social services," participation (but who knows to what extent) in a homeownership program, etc.

g. 96-32's "other" provisions, like the "facts and circumstances" provisions, provide organizations yet another way to avoid the safe-harbor requirements (income limits). An organization might satisfy 96-32 by "combating community deterioration,"or by "lessening government burdens,"or by "eliminating discrimination and prejudice,"or by "lessening neighborhood tensions,"or by "relieving distress of the elderly or physically handicapped." This last category cross-references IRS Rev. Rul. 72-124, 79-18, and 79-19. This last category thus would bring us right back to financial prescreening so only those who can afford admittance get admitted.

h. 96-32 does provide that if an organization furthers private interests of those with a financial stake in the project, that could cause an organization to fail to qualify for IRS exemption. Might, for example, a 90% refundable endowment fee at a high-end-senior-independent-living facility already run afoul of this private-interest restriction?

4. In light of the above items a-g, IRP 96-32 is not the answer to making 70.11(4) more clear and workable, and more uniform in Wisconsin for our property-tax system.

5. Note that the Legislative Council, in the drafts at our last Committee meeting (0078/1 and 0082/P1), had references to **IRS Ruling 72124 (72-124)** (**copy attached**), and note that, as reflected in the latest drafts (0086/1 and 0090/1), the Legislative Council is no longer relying upon and adopting 72-124. Consequently, if IRS 72-124 is being rejected, then IRP 96-32 must be rejected because, as alluded to above, IRP 96-32 sweeps in and embraces 72-124 as an alterantive permissible way to get IRS exemption even if the poor are not being served. See, e.g., 96-32 § 3.02(4), § 6.01(5). Thus, if IRP 96-32 were adopted in Wisconsin as a property-tax-exemption device, Wisconsin would still be confronted by IRS-income-tax-exempt-nonprofit facilities being exempt who screen out the poor and who only admit those who can afford to get in and stay in, and who charge entrance fees and monthly fees. See IRS 72-124 attached, and Year 2000 Government-5 Legislative Taskforce Report § X.

6. Any **PILOT** requirement should be a PILOT like the one the state already mandates for public housing authorities (City rate x mkt value = PILOT) (see 70.11(18) and 66.1201(22)) and redevelopment authorities (66.1333(12)) rather than being a fee for municipal services actually furnished to the property. Cities already have service-fee powers under 66.0627.

7. If the State is going to give relief to exempt owners from the "**rent-use requirement**," any such relief must be narrowly crafted and clarify that the owner must use the income to further the benevolent owner's activities AT THE PROPERTY. When a nonprofit uses one parcel as a cash cow to subsidize a completely different parcel, the probability is high that the activity at the cash-producing parcel is in direct competition with property-and-income-taxpaying-for-profit entities.

8. Perhaps the **subcategory 1-4 exemptions** in 0086/1 and 0090/1 for nursing homes, CBRF's, adult family homes, and RCAC's are fine. They appear to be. But, the Committee has not heard any testimony on these. For example, are there for-profit RCAC's in competition with nonprofit RCAC's? Are there "nonprofit" RCAC's that accept only private pay residents at market rates that would be unaffordable to truly low income people?

9. Consistent with my Memo 4, and to avoid the problems associated with IRP 96-32, I would suggest that the subcategory 7 and 8 exemptions in 0086/1 and 0090/1 be eliminated and replaced with "residential housing to the extent that occupants have household income limits at or below the **homestead limit** of $24,500." I would allow for partial exemptions.

   A December 16, 2004 Milwaukee Journal Sentinel article (Avrum Lank and Steve Walters), entitled, "State spreads tax burden" discussed the "first report in

25 years examining who pays Wisconsin taxes..." authored by the Dept. of Revenue. "Overall, property and sales taxes tend to hit low-income households hardest but are 'offset' by deductions, graduated tax rates and breaks built into the state income tax system..." like the homestead credit. The homestead-credit concept could thus be extended further from the income-tax arena to the property-tax arena to make our system more fair.

Per the DOR Report (Tax Incidence Study): the median income for elderly households (65 years old) in Wisconsin is $23,100; the poorest 20% of Wisconsin's households have income up to $15,600; and the second poorest 20% have incomes from $15,601 to $27,900. Thus the $24,500 homestead-credit limit, if adopted as a 70.11(4)-benevolent-association-income limit, would help each of Wisconsin's elderly and Wisconsin's poor who live in nonprofit housing.

96-32 "Safeharbor" example. In the City of Milwaukee, for a family of four, per HUD's January 28, 2004 data, under IRP 96-32, "very low income" = 50% AMI[1] = $33,600, and "low income" = 80% AMI = $53,750. Thus, a 24-unit-nonprofit-apartment building would be exempt under 0086/1, 70.11(4)(c)7 or 0090/1, 70.11(4)(c)7 (i.e. benevolent-association housing for low-income persons operated in compliance with IRP 96-32) IF:

> 18 units (75% of the units = 24 x .75 = 18 units) are occupied by those at or below $53,750
>
> AND
>
> EITHER 4.8 units (20% of the units = 24 x .20 = 4.8 units) are occupied by those at or below $33,600
>
> OR
>
> 9.6 units (40% of the units = 24 x .40 = 9.6 units) are occupied by those at or below $40,320.

The Legislative Council drafts would thus exempt a nonprofit, 24-unit complex where most units are at or below $53,750.

Per the DOR Report, $55,709 is the third from the top of household average income in Wisconsin, so the $53,750 would grant exemption to middle income occupants. And, with IRP 96-32's "other" and "facts and circumstances" ways

[1] AMI means area median income.

to sidestep the 96-32 "safeharbor" income limits, actual income of occupants exempt under the Legislative Council drafts (adopting 96-32) could actually be much higher. In deed, nonprofit elderly housing could, under 96-32, with its cross reference to IRS 72-124, disregard the 96-32-safeharbor-income limits altogether and continue to prescreen applicants for wealth.

10. Even if the Committee determines to not accept the above, and if it wishes to proceed with one or the other of the Legis. Council's drafts, I have specific language changes that I will offer. For example, the addition of certain commas, cross-references, clarifiers, etc.

C. WISCONSIN PUBLIC POLICY.

1. Under existing Wisconsin law, a "benevolent association" exemption should only go to an entity that predominantly benefits the public at large, or an "**indefinite class**" of people. Thus, under existing law, it is foreseeable that those "nonprofits" that currently and predominantly serve their own members, as opposed to an indefinite class, would lose their exemption. That is, after litigation and court cases, there would be no exemption for high-end-senior-independent-living facilities that operate within IRS guidelines, that prescreen to ensure only financially able are admitted, and that build-up reserves for the few instances where the prescreening might not work (i.e.a prescreened applicant may actually run out of cash and have to use the reserves). This is the conclusion recently reached by courts in West Virginia, Illinois, Pennsylvania, and Massachusetts. *Maplewood Community, Inc. v. Craig,* 2004 WL 2579292 (Supr. Ct. of Appeals, W. VA, Nov. 12, 2004); *Eden Retirement Center, Inc. v. Dept. of Revenue,* 2004 WL 2745641 (Supr. Ct. IL, Dec. 2, 2004); *Jewish Geriatric Services, Inc. v. Board of Assessors of Longmeadow,* 61 Mass. App. Ct. 73, 807 N.W.2d 194 (April 30, 2004), *Alliance Home of Carlisle, PN v. Board of Assessment Appeals,* 852 A2d 428 (Commonwealth Ct. of PN, June 15, 2004). See, also, B.3.g. above – one could argue that a refundable endowment fee runs afoul of the IRS-private-interest restriction.

2. If the law is to be changed, it should be changed: to make Wisconsin's property-tax system more fair for ALL, including those who own and rent and live in nonexempt housing and who will thus have to subsidize those fortunate enough to be exempt; to remove the disparity and unfairness under current exemption law whereby low-income persons are screened out and not admitted to exempt facilities serving the wealthy; to encourage homeownership by property-taxpaying owners; and to establish a bright-line standard that assessors and owners will readily understand, and be able to follow.

ATTACHMENTS: IRP 96-32

IRS 72-124

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