

Taxing times

Real estate slump robs city of \$30M in transfer fees

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Baltimore pulled in \$30 million less in much-needed tax revenue from commercial and real estate sales in the past year, a drop that could reverse a decade-old renaissance that brought with it new developments and city dwellers.

Transfer and recordation taxes — money the city gets when real estate is sold or property owners get mortgages or construction loans — fell to \$47 million. That's down from nearly \$76 million in 2008 and from \$116.7 million at the market's peak in 2006, according to city budget data.

The dramatic drop already has prompted City Hall to cut city services and is thwarting efforts to decrease the residential property tax rate, still the highest in Maryland. City officials are left with finding new sources of revenue and figuring out how to reduce an increasing burden on city homeowners.

Compounding the problem is the fact that many commercial and residential real estate projects —

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McHenry Row in Locust Point and the east-side biotechnology park among them — that could generate new tax income for the city have stalled or been delayed in the recession. And without financial assistance from leery investors or state or federal programs, those projects are not moving forward soon.

"You're sort of hitting, almost, a perfect storm in the city," said Donald C. Fry, president of the Greater Baltimore Committee, a business advocacy group. "One of the biggest challenges for Baltimore City has always been the high property tax rate, the disproportionately high tax rate compared to many other jurisdictions."

Taking on taxes

Mayor Sheila Dixon said there is not much the city can do in the short term to replace the lost revenue. She can't convince banks to start lending again, leaving the city at the mercy of tighter lending standards.

Still, Dixon said she remains committed to bringing down the property tax rate. That rate is \$2.27 for every \$100 of

assessed property. Baltimore County's tax rate is \$1.10 for every \$100 of assessed property.

To generate revenue, Baltimore is trying to help developers get their projects on track by issuing public debt to cover the difference between what developers can borrow for their projects and how much more they need. Those new projects, like Patrick Turner's planned \$1.4 billion Westport development, will bring more tax revenue to the city and give Baltimore leaders the financial flexibility to bring property taxes down, Dixon said.

"We take one project, one initiative at a time, to try to figure out if we can help fill the gap or take some of those risks," Dixon said.

But many of those projects, including Westport, aren't far enough along to start generating new taxes for the city. That forced Baltimore to cut \$65 million from its budget, reducing trash collection, summer programs, fire companies, libraries and recreation centers. The \$1.4 billion redevelopment of State Center in midtown Baltimore, a 3,750-machine slots parlor near M&T Bank Stadium, and additional development at Harbor Point are also projects the city is counting on for additional tax money.

A city task force in 2007 called for a 32 percent reduction in the property tax rate, which would have brought the city's tax rate closer to those of its surrounding counties. The committee warned the disparity in tax rates might cause a property owner to think twice about buying in the city, while lowering the tax rate could help drive new growth and development in Baltimore.

Since then, however, City Hall has not acted on the recommendation. The recession put a halt to any tax rate relief.

Meanwhile, decimated tax revenue is affecting local governments across Greater Baltimore and nationally, as the credit crunch has stalled new construction projects and made it hard for investors and hopeful homeowners alike to borrow money. The crisis has left many of the nation's largest cities with budget



shortfalls of more than \$100 million, according to a June 12 report from the U.S. Conference of Mayors.

As in Baltimore, cities like Boston, Denver, Kansas City, Mo., and Philadelphia have enacted hiring freezes, employee furloughs, pay and benefit cuts and increases in fees and charges to overcome their deficits.

"The recession is having a pretty amazing impact on those cities in terms of their economic developments," said Eugene T. Lowe, assistant executive director at the U.S. Conference of Mayors. "There was a lot of energy before that. Whether that's all gone and can't be picked back up, it remains to be seen."

Falling revenue

In Baltimore, the economic downturn dragged down nearly all of the city's largest revenue streams in the past year, from hotel and income taxes to its own investments. But the sharpest decline was in transfer and recordation taxes, a sign of how deeply the real estate slump has settled over Baltimore.

The city collected \$20.5 million less in transfer and recordation taxes from residential property sales in the past year. Commercial property sales taxes were down about \$8.3 million.

The city's real estate market hasn't dried up completely, but fewer deals are getting done and for less money. About 1,900 commercial properties sold in the city's 2008 fiscal year, generating about \$20.7 million in transfer and recordation taxes. For the year ended June 30, 700 fewer properties traded hands, bringing about \$12.4 million in taxes to the city.

Most of those deals aren't for large office towers, bought by private investors or pension funds as in the past, but for smaller buildings bought by busi-

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nesses looking to trade in their rental payments for mortgages. Among them is PLDA Inc., a city interior design and architecture firm that recently bought a 5,000-square-foot brownstone in the city's Mount Vernon neighborhood for less than \$1 million.

The St. Paul Street building was one of two bought previously by Tower Hill Development and planned for an office and condominium project that never caught on. PLDA plans use the building for its

offices and rent some of its excess space to at least one other tenant.

PLDA Principal Barbara Portnoy said moving out of the city was never a consideration for her, but she noted she would have looked at other properties had it not been for a tax credit on the building that will cap property tax increases for the next 10 years.

"There was no consideration of leaving the city; there's a sense of excitement and energy of being in the city," she said.

On the residential side, fewer than 10,400 homes sold from June 2008 to June 2009, generating about \$34.4 million in sales taxes. That's compared with nearly 14,200 properties sold in fiscal 2008, bringing nearly \$55 million in taxes to the city.

"It's a pretty bleak picture," said Joseph T. "Jody" Landers, executive vice president of the Greater Baltimore Board of Realtors. "I'm hoping what we're seeing is relatively short-lived."

Landers said he believes the market will continue to slow as more companies shed workers in Greater Baltimore. With so much uncertainty, Landers said, many hopeful homebuyers remain reluctant to take on a new mortgage for fear of losing their jobs.

It's the high property tax rate that could make it tougher for the city's real estate market to recover. Every dollar counts for prospective homebuyers in this market. Existing homeowners also are feeling the pinch, as the housing bubble of just a couple years ago sent home prices soaring. That has meant higher assessments on property.

Residents in South Baltimore will see their property taxes increase by an average of 7 percent a year, or 21 percent over the next three years. The city is projecting \$42.5 million more in property taxes this year, with 40 percent of that increase from reassessments.

"I think the tax situation always plays on people's minds," said Landers, also co-chair of the city tax reform panel. "Now I think it's having a really hard impact on the city market in particular."

According to Dixon's tax reform committee, the owner of a home assessed at \$150,000 pays up to \$3,402 in city taxes, compared with \$1,650 in Baltimore County. Likewise, a commercial property assessed at \$25 million carries an annual city tax bill of \$567,000 but would be

charged \$276,000 in Baltimore County.

Feeling the burden

A high property tax rate creates an even tougher sell for Baltimore-area homebuilders like the Dominion Group, Partner Jack Bevier said. Dominion has about 350 properties in the city, many of which it hasn't been able to sell because of the real estate slump. That means the company is carrying a significant amount of inventory, and rising assessments on many of those properties will drive up Dominion's carrying costs.

But even with those challenges, Bevier said, Dominion believes there is still an interest in city living and the group is continuing to seek investment opportunities in Baltimore.

"We're going to be here for the long term," he said.

Others aren't so sold on city living, or at least the cost of it.

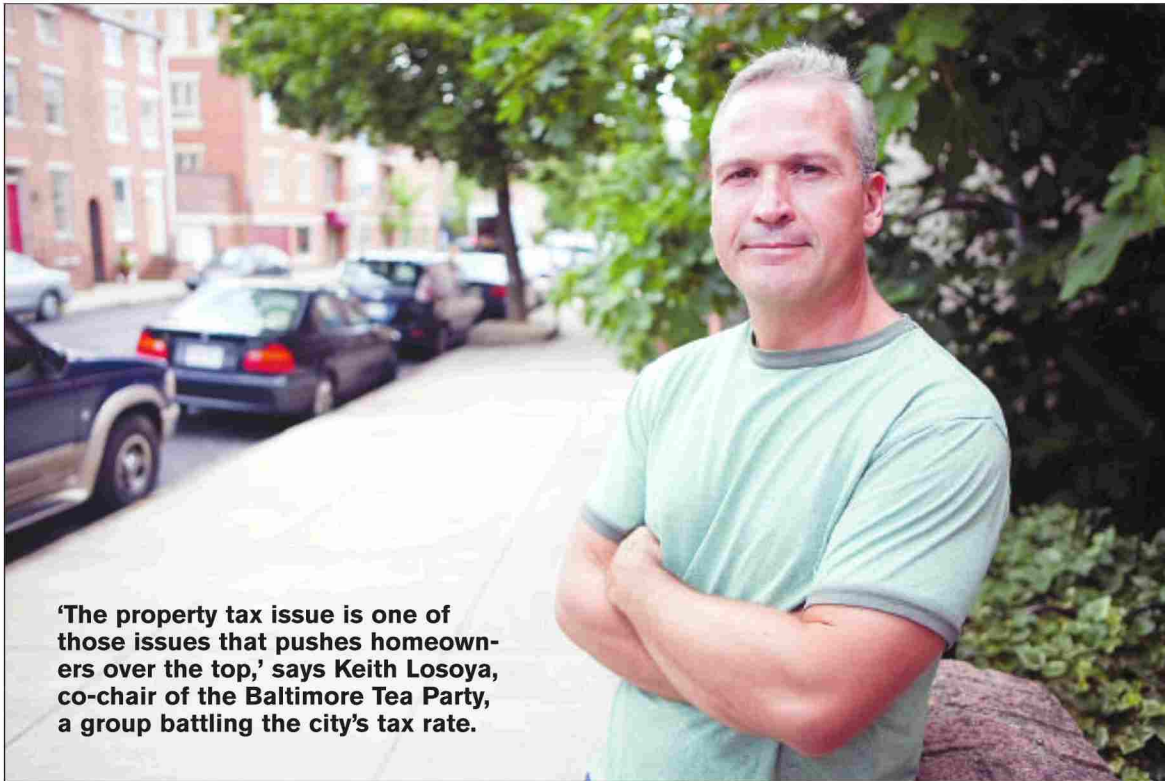
"The property tax issue is one of those issues that pushes homeowners over the

top," said Keith Losoya, a Federal Hill resident and co-chair of the Baltimore Tea Party, which lobbied City Hall for property tax relief earlier this year.

Losoya said he believes the city's tax rate could drive homeowners out of Baltimore if it isn't lowered.

More of a fear is that a flight of property owners to the surrounding counties could prompt some businesses to relocate, too. That's particularly harmful at a time when the city needs more residents and employers to expand its tax base and bring property tax rates down.

"This is the reality of Baltimore City, and is one of the reasons that the city must eventually become more competitive relative to the counties with regard to its property tax rate," said economist Anirban Basu, CEO of the Sage Policy Group and a Baltimore City Public Schools board member. "Eventually may not be soon enough, at least to preserve significant aspects of this decade's renaissance."

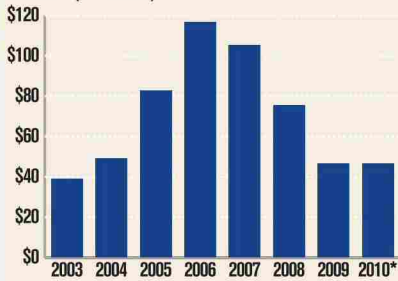


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Free Fall

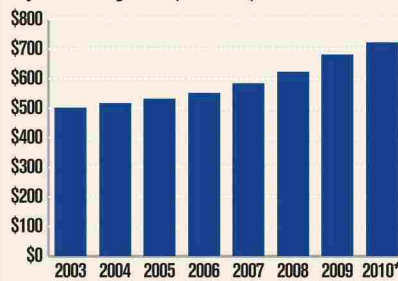
A big drop in commercial and residential real estate sales has decimated recordation and transfer tax revenue (in millions).



*Projected for fiscal year.
 Source: Baltimore City budget office

A Growing Burden

Increased assessments on city property pushed tax revenue up amid worries that the higher taxes would stymie future growth (in millions).



*Projected
 Source: Baltimore City budget office



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Despite high property taxes, Barbara Portnoy didn't want to leave the city.