

Recordation Tax Material

*Please bring the packet from the May 8 Management and Fiscal Policy Committee meeting (item 1).*

**MEMORANDUM**

TO: County Council

FROM: Michael Faden, Senior Legislative Attorney

SUBJECT: **Action:** Emergency Bill 7-02, Recordation Tax - Rates and Exemption

**Management and Fiscal Policy Committee recommendation: enact with amendments.**

At its worksession on May 8, the Management and Fiscal Policy Committee unanimously recommended the following amendments to Bill 7-02 (see ©1-3):

- Set the tax rate at \$3.45/500 (\$6.90/1000) and the exemption for owner-occupied housing at the first \$50,000. This results in a break-even point of \$138,000 and estimated increased revenues of \$16 million in FY03 up to \$22.2 million in FY08.
- Applied the new rate and exemption to transactions that occur on or after July 1, 2002 (not, as in the introduced bill, documents recorded on or after that date).
- Designated the net added revenue to be used for capital improvements to schools and educational technology for Montgomery College.

*Please retain this packet for the May 9 Council session (item 5).*

## MEMORANDUM

TO: Management and Fiscal Policy Committee

FROM: Michael Faden, Senior Legislative Attorney

SUBJECT: **Worksession:** Emergency Bill 7-02, Recordation Tax - Rates and Exemption

Councilmember Subin, Council President Silverman, and Councilmember Praisner introduced Emergency Bill 7-02, *Recordation Tax - Rates and Exemption*, on March 19. A public hearing was held on April 23 (see testimony, ©9-19). At a worksession on April 29, this Committee discussed several issues but did not make a final recommendation on this bill. The issues on which the Committee adopted recommendations are noted below.

**Summary** The purpose of Bill 7-02 is to raise significant amounts of revenue for school capacity construction while making the County recordation tax more progressive, and thus making lower-priced housing more affordable. This bill would increase the rate of the County recordation tax from \$2.20/\$500 to \$4.50/\$500 (\$4.40 to \$9/\$1000 -- in percentage terms, from 0.44 to 0.9%), which is a 104.5% increase.<sup>1</sup> The bill also exempts from the tax the first \$115,000 of consideration for an owner-occupied residence. This is the only exemption that Council staff believes is allowed by the state law which authorizes counties to levy the recordation tax (see state law, ©5). The effect of this exemption and the higher rate, as shown in the tax rate table on ©6, is to reduce the tax on any house worth less than \$225,000, which is slightly below the most recent median price of a single-family house in the County. As introduced, Bill 7-02 would commit the Council to allocate the revenue raised by the higher tax rate to construct new schools and additions to existing schools. See ©2, lines 24-27.

**Revenue estimates** OMB and Finance Department staff estimated the added revenue from the various proposals in amounts ranging from \$20.8 million to \$15 million in FY03. See fiscal impact statement on ©22, explanation on ©23, and estimates of various options on ©24-

<sup>1</sup>At the first MFP worksession on April 29, Committee Chair Praisner asked whether this tax rate could be set by Council resolution without Executive approval, as the property tax and certain excise taxes are. While the issue is definitely not free from doubt, Council and County Attorney staff concur that, because the applicable state law (Tax-Property §12-103; see ©5) requires this tax rate, unlike others, to be set "by law", that phrase would probably be construed to require the use of a process which gives the Executive veto authority over the rate set. This result is likely even though the term "governing body" as defined in the Tax-Property article (§1-101(n)), can and probably should be construed, as it relates to setting tax rates, as meaning only the Council under County Charter §305.

25. Council staff continues to caution Committee members that, because the yield from this tax is relatively unpredictable from year to year, all of the estimated added revenues should not be relied on to support any high-priority expenditures.

### Issues

**Rate and exemption** The following table compares the proposals offered so far, and others noted by staff:

Proposal	Tax rate (\$ per \$1000)	Percentage increase in rate	Exemption (first \$ of consideration)	Break-even point (\$)	Estimated added revenue (\$) in FY03*
<b>Bill 7-02 as introduced</b>	9	104.5	115,000	225,000	20,800,000
<i>Previous bills:</i>					
<b>Bill 14-01</b>	6.60	50	40,000	120,000	15,000,000
<b>Subin amendment to bill 14-01</b>	6.90	56.8	55,000	151,800	15,300,000
<b>Bill 30-01**</b>	4.95	12.5	35,000	315,000	1,400,000
<i>Bill 7-02 alternatives (listed in order of progressivity):</i>					
<b>Taxpayers League##</b>	9	104.5	142,750	279,293	15,400,000
<b>Subin amendment#</b>	7.50	70.5	72,000	174,194	17,400,000
<b>GCAAR</b>				150,000	
<b>Staff option 1</b>	6.90	56.8	50,000	138,000	16,000,000
<b>Staff option 2</b>	6.90	56.8	45,000	124,200	16,800,000
<b>MNCBIA</b>	6.60	50	40,000	120,000	15,000,000

\*OMB/Finance staff estimate.

\*\*Still pending

#Announced at April 23 public hearing.

##See ©9, 11.

This table illustrates the 3-way relationship between the tax rate, the exemption level (if any), and the break-even point (the highest sale amount at which the tax would not increase; sometimes referred to as the "neutral price" or "tipping point"), and the similar dynamic relationship between the rate, exemption level and revenue yield. In our view, an effective way for the Committee to sort these factors out is to decide first on a **revenue yield** target, and then

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on the **break-even point** (the level of progressivity to be achieved). Once those decisions are made, calculating the rate and exemption amount becomes essentially a matter of reworking the spreadsheet developed by Council staff (see example on ©21).<sup>2</sup>

In discussing **revenue yield**, the Committee should remember that the recordation tax is a relatively volatile revenue source, fluctuating significantly by economic activity and particularly the level of home sales in the County; thus any revenue estimates are somewhat crude forecasts and cannot be relied on precisely. (The tax rate level influences the revenue yield more than the exemption level because the rate applies to many transactions -- Finance staff estimates about 30% of the total<sup>3</sup> -- that do not qualify for the exemption because they involve other than owner-occupied residences.) To budget conservatively for tangible needs such as school construction, Council staff recommends that the Committee use the OMB/Finance estimates in the table on page 2 as a *best-case* revenue scenario.

In considering the degree of progressivity to be achieved (as measured by the **break-even point**), the central policy issue seems to be *how much to shift the burden of this tax from buyers of moderate-priced houses to buyers of high-end houses*. In Bill 7-02 as introduced the break-even point is \$225,000, which is slightly below \$238,000, the most recent median price for single-family houses.<sup>4</sup> As the table on ©6 shows, the formula in Bill 7-02 would increase the tax paid by the buyer<sup>5</sup> of a \$1 million house by \$3565, which arguably is easily bearable at that income level and relatively less of a burden than a smaller increase paid by a moderate-income buyer. While the *nominal rate* would still be \$9, the \$115,000 exemption would reduce the *effective rate* at the \$1 million level to \$7.96/1000.<sup>6</sup> On the other hand, some realtors and others have objected to making the tax progressive, or at least markedly so, urging that a level rate is fairest to all homebuyers (see, e.g., testimony, ©18-19).

Another factor in setting the tax rate is comparability with surrounding jurisdictions. For details of the rates in other Maryland counties, see ©7-8 (note that the rates in these tables are per \$500). The recordation tax in the District of Columbia is 1.1% (\$11/1000), along with a transfer tax of the same amount. The recordation tax in nearby Virginia counties at last report is \$5/1000 (\$3 on the deed and \$2 on the mortgage). Even at the \$9/1000 nominal rate proposed in Bill 7-02, the County's rate would be less than Frederick County's rate of \$10, although Frederick County does not levy a county transfer tax.

**Sunset** In their testimony (see ©12-15), both Maryland-National Capital Building Industry Association and Greater Capital Area Association of Realtors proposed a 3-year sunset for the rate and exemption in this bill. If that sunset date were adopted, the FY 2003-8 Capital

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<sup>2</sup>The tax rate would, of course, apply to commercial as well as residential transactions. The state law (see ©5) appears to allow only a single tax rate in each jurisdiction. An attempt to change the state law to allow more than one rate did not get off the ground in the last legislative session. At the previous worksession Committee Chair Praisner noted that the County could subsidize deserving businesses through the Economic Development Fund.

<sup>3</sup>See Finance staff explanation on ©23.

<sup>4</sup>*Economic Forces that Shape Montgomery County (Update 2002)*, produced by Research and Technology Center, County Department of Park and Planning, March 2002, pp. 12, 29.

<sup>5</sup>Assuming the buyer pays the entire tax; normally the seller and buyer split it, although economists would argue that the seller then simply locks it into the price of the house.

<sup>6</sup>To compare the effective rates of some options in the table on page 2, see the Council staff spreadsheet on ©26.

Improvements Program could only count the added revenue from this tax during the first 3 fiscal years. **Committee recommendation:** do not sunset the tax rate or exemption.

**Use of funds** As introduced, Bill 7-02 includes an "intent of the Council" provision that would direct the added revenue attributable to the higher tax rate to construct new schools and additions to existing schools. See ©2, lines 24-27; also note MCPS letter on ©20. **Committee recommendation:** broaden this provision to allow the net added revenue to be used for any public school capital improvement, including school modernization, and for educational technology. The final decisions on use of these funds would still be made in the capital and operating budgets, and were discussed recently by the Council's Education Committee.

**Effective date** As introduced, Bill 7-02 is an Emergency bill and would take effect on July 1, 2002, applying to all documents recorded on and after that date. **Committee recommendation:** keep the July 1 effective date. After the Committee worksession GCAAR staff expressed concern about possible delays in recording documents from property settlements that occur in June, thus resulting in the higher rate being applied "retroactively". Council staff plans to discuss this issue with the Clerk of the Circuit Court to see whether any lag time in late June can be minimized.

This packet contains:

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Emergency Bill No. 7-02  
Concerning: Recordation Tax - Rates  
and Exemption  
Revised: 5-8-02 Draft No. 2  
Introduced: March 19, 2002  
Enacted: May 9, 2002  
Executive: \_\_\_\_\_  
Effective: July 1, 2002  
Sunset Date: None  
Ch. \_\_\_\_\_, Laws of Mont. Co. \_\_\_\_\_

## COUNTY COUNCIL FOR MONTGOMERY COUNTY, MARYLAND

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By: Councilmember Subin, Council President Silverman, and Councilmember Praisner

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### AN EMERGENCY ACT to:

- (1) increase the rate of the recordation tax;
- (2) exempt a certain amount of the consideration for an owner-occupied residential property from the recordation tax;
- (3) confirm certain actions previously taken regarding the recordation tax;
- (4) declare the intent of the Council regarding the use of certain revenue from the recordation tax; and
- (5) generally amend County law affecting the recordation tax.

By adding

Montgomery County Code  
Chapter 52, Taxation  
Section 52-16B

<b>Boldface</b>	<i>Heading or defined term.</i>
<u>Underlining</u>	<i>Added to existing law by original bill.</i>
[Single boldface brackets]	<i>Deleted from existing law by original bill.</i>
<u>Double underlining</u>	<i>Added by amendment.</i>
[[Double boldface brackets]]	<i>Deleted from existing law or the bill by amendment.</i>
* * *	<i>Existing law unaffected by bill.</i>

*The County Council for Montgomery County, Maryland approves the following Act:*

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1           **Sec. 1.       Section 52-16B is added as follows:**

2   **52-16B.       [Reserved] Recordation Tax**

3           (a)   Rate. The rate of the recordation tax, levied under state law, is  
 4                [[~~\$4.50~~]] \$3.45 for each \$500 or fraction of \$500 of consideration  
 5                payable or of the principal amount of the debt secured for an  
 6                instrument of writing, including the amount of any mortgage or deed  
 7                of trust assumed by a grantee.

8           (b)   Exemption. The first [[~~\$115,000~~]] \$50,000 of the consideration  
 9                payable on the conveyance of any owner-occupied residential  
 10               property is exempt from the recordation tax if the buyer of that  
 11               property intends to use the property as the buyer's principal residence  
 12               by actually occupying the residence for at least 7 months of the 12-  
 13               month period immediately after the property is conveyed.

14           **Sec. 2.       Emergency Effective Date.**

15           The Council declares that an emergency exists and that this legislation is  
 16           necessary for the immediate protection of the public health and safety. This Act  
 17           takes effect on July 1, 2002, and applies to any [[instrument recorded with the  
 18           Clerk of the Circuit Court]] transaction that occurs on or after that date.

19           **Sec. 3.       Effect of Previous Actions.**

20           [[This]] Effective July 1, 2002, this Act supersedes Resolution No. 7-182[[,  
 21           effective July 1, 2002]]]. Any action taken under that resolution before that date,  
 22           including the levy and collection of the recordation tax, is ratified and confirmed as  
 23           if that action had been taken under authority of a law enacted by the County  
 24           Council.

25           **Sec. 4.       Allocation of Revenue.**

26           The Council intends to allocate the net revenue attributable to the increase in  
 27           the rate of the recordation tax enacted in this Act to the cost of [[constructing new



28 schools and additions to existing]] capital improvements to schools and  
29 educational technology for Montgomery College.

30 *Approved:*

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Steven A. Silverman, President, County Council Date

32 *Approved:*

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Douglas M. Duncan, County Executive Date

34 *This is a correct copy of Council action.*

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Mary A. Edgar, CMC, Clerk of the Council Date

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THE MARYLAND-NATIONAL CAPITAL PARK AND PLANNING COMMISSION

**MCPB**  
**7/31/03**  
**Items #2 and 3**

**MEMORANDUM**

**TO:** Montgomery County Planning Board

**FROM:** Community – Based Planning Division

**SUBJECT:** Preliminary Forest Conservation Plan  
Board of Appeals Petition No. S-1565-A (Special Exception Modification)

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The staff report for the above-cited items will be delivered to the Planning Board on Monday, July 28, 2003.