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States and Cities May Need Shelter From the Storm Brewing in U.S. Housing Policy.

Changes are likely on the way, and they could damage budgets.

The direction set by Ben Carson, the new Department of Housing and Urban Development secretary, will have immense impacts on localities. For starters, federal housing programs make up 40 percent of federal transfers to local governments. That's a big chunk of change even as federal transfers overall have been in a long-term decline.

Before we go on, here are some key numbers: Since 1977, the share of local government revenue from non-tax sources has remained fairly steady at 60 percent of general revenue. But the composition of non-tax revenue has changed. The portion from intergovernmental transfers declined from 43 percent of general revenue in 1977 to 36 percent in 2013, while revenue from charges and fees increased from 15 percent to 23 percent. Likewise, while the share of general revenue from local taxes has remained at about 40 percent, the composition of tax revenue has changed. The contribution of property taxes to general revenue declined from 34 percent in 1977 to 30 percent in 2013, while revenue from sales taxes increased from 5 percent to 7 percent.

Bottom line: Whether or not Carson makes any changes to federal transfer monies, the pressure on local taxes is real. On property taxes, the least popular of the three possible local taxes, the pressure is especially immense.

Consider Pennsylvania. In January, Gov. Tom Wolf recommended a three-pronged approach to helping distressed cities. Along with state economic aid and easing municipal pension debt, he suggested providing property tax relief. If his plan is successful — and legislators in Harrisburg seem open to it — it would help city residents by cutting the biggest single local tax bill they pay. "Places like Scranton would see a big drop in the tax bill and a big increase in property values," the governor told The Scranton Times-Tribune. His January comments came in the wake of action taken by the Pennsylvania House, which passed a bill to replace nearly \$5 billion worth of property taxes with higher state income and sales taxes. The state Senate narrowly rejected a bill to mostly eliminate property taxes with that same combination of higher state taxes.

Once localities are dependent on state taxes — rather than property tax revenue — they are at greater peril. The property tax may have its up and downs, but it is by and large a fairly steady income stream and one that's under a locality's control. State payouts are prey to budget cuts when there's a downturn in the economy.

The affordability of housing, which also has a huge impact on localities, is spiraling in an unfortunate direction. Mortgage rates have been on the rise and are likely to continue to inch up. Federal policy could be a further threat. Both the mortgage-interest deduction from federal income taxes and tax-exempt housing bonds are at risk in the new Congress. Meanwhile, the nation's housing inventory is nearly 10 percent below a year ago, and the homeownership rate has fallen close to a 51-year low.

Rental affordability is an even bigger problem. Between 2001 and 2013, we lost 2.4 million rental

housing units (both market-rate and subsidized) that were affordable to people making less than 50 percent of area median income. In addition, 106,000 public housing units and 146,000 project-based rental assistance units were lost, according to an Urban Institute report, which also noted that some 450,000 more units are at risk of disappearing or deteriorating.

Building more units or preserving existing ones would help, but with a very large federal deficit, and proposed steep federal tax cuts, it appears unlikely that traditional HUD programs will be able to fill the gap. Chances are that HUD will experience significant budget cuts, which means both Community Development block grants and housing assistance to states and localities will be diminished.

That's not a pretty housing picture for cities, their pocketbooks and their housing stock.

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