Action Item # 6059/22
Docket Date: April 13, 2022

City of Newport

REQUEST FOR CITY COUNCIL ACTION

To:	**Mayor Jeanne-Marie Napolitano & Members of the City Council**
From:	**Joseph J. Nicholson, Jr., Esq., City Manager**
Date:	**April 5, 2022**
Subject:	**Interim Report of the Taxation Relief Ad Hoc Committee and Request to the State Legislative Delegation to Introduce Legislation to the General Assembly for a Proposed Amendment to Section 44-5-76.1 of the Rhode Island General Laws**

RECOMMENDATION:

It is recommended that the Council receive the attached Interim Report from the Taxation Relief Ad Hoc Committee and adopt the attached resolution requesting that Newport's Legislative Delegation introduce the appropriate legislation to the Rhode Island General Assembly to amend Section 44-5-76.1 of the General Laws allowing the City to adopt a split tax rate for its class 2 residential real estate for owner and non-owner occupied properties.

BACKGROUND AND FINDINGS:

The City Council, via Resolution 2021-49, tasked the Taxation Relief Ad Hoc Committee with the following:

> "This committee shall further review and investigate property tax relief for Newport residents and be comprised of members of the City administration who are familiar with taxation and exemptions and five members of the community, all who have a background in, and knowledge of finance, and preferably familiar with municipal property taxation.
>
> This committee shall have the authority to hold meetings, conduct interviews, collect data, review ordinances and plans established by other communities and shall formulate a report to the Council with its findings and recommendations. The Committee shall have six months to perform this service and to present the council with its report."

The Committee has completed an interim report which suggests to the Council that they seek legislative authority to adopt a split tax rate system to implement if Council so desires.

PREVIOUS LEGISLATIVE ACTION

Resolution 2021-49 – Creating Taxation Relief Ad Hoc Committee

FISCAL IMPACT

___ Currently Budgeted (Account _________________) ___ Requires additional appropriation ___ No Fiscal Impact

SUPPORTING DOCUMENTS

Resolution with Proposed Amendment to Section 44-5-76.1 of the RI General Laws
Interim Report of the Ad Hoc Tax Relief Committee

Finance Dept. Review: _____ Date By: _________ (if applicable)

THE CITY OF NEWPORT

RESOLUTION
OF THE
COUNCIL
No.

WHEREAS: The City of Newport wishes to adopt revisions to its tax classification of properties to provide for a split tax rate for its Class 2 residential real estate for owner and non-owner occupied properties in order to provide property tax relief to its year-round residents; and

WHEREAS: Such revisions require the passage of enabling legislation by the General Assembly.

NOW THEREFORE, BE IT

RESOLVED: that the City Council of the City of Newport requests the Rhode Island General Assembly to adopt and ratify the proposed amendment to Section 44-5-76.1 of the General Laws entitled "Newport – Property tax classification – List of ratable property", attached hereto; and

BE IT FURTHER

RESOLVED: that copies of this Resolution be forwarded to the City of Newport's Legislative Delegation requesting that they introduce the appropriate legislation and work for its passage in the 2022 session of the General Assembly.

IN COUNCIL
READ AND PASSED

____
LAURA C. SWISTAK
CITY CLERK

AN ACT

RELATING TO TAXATION – TAX CLASSIFICATION PLAN IN THE CITY OF NEWPORT

<u>Introduced By:</u>

<u>Date Introduced:</u>

It is enacted by the General Assembly as follows:

SECTION 1. Section 44-5-76.1 of the General Laws entitled "Newport – Property Tax Classification – List of ratable property" is hereby amended as follows:

Upon adoption of a system of classification of taxable property by the city of Newport, all ratable property in the city of Newport shall be classified by the assessor as follows:

(1) Class One: all ratable tangible personal property;

(2) Class Two: residential real estate with less than four (4) units;

(3) Class Three: all commercial and industrial real estate and residential real estate with four (4) units or more; and

(4) Class Four: motor vehicles and trailers subject to the excise tax created by chapter 34 of this title.

<u>In lieu of the City of Newport adopting a homestead exemption authorized by ordinances enacted pursuant to the provisions of §44-5-78, the City of Newport may divide the residential real estate class into non-owner and owner occupied property and adopt separate tax rates in compliance with the restrictions set forth in §44-5-76.2. The City of Newport by resolution or ordinance may provide rules and regulations governing the same, including but not limited to what constitutes non-owner and owner occupied property.</u>

SECTION 2. This act shall take effect upon passage.

Date: March 15, 2022

To: Newport City Council

From: Ad Hoc Tax Relief Committee

Re: Interim Progress Report

Committee Membership	*Meetings Held*
Atkins, Mary Ellen	October 28, 2021
Behan, Christopher	November 4, 2021
Booth, Allan	November 18, 2021
Hunt, Penelope	December 2, 2021
Nicholson, Joseph	January 13, 2022
Nolan, James	January 27, 2022
Phillips, Jade	February 10, 2022
Skuncik, Caroline	March 10, 2022
Sitron, Laura	
Urban, Kenneth	

Goal Setting
The committee identified the following goals of its work:

- Provide tax relief to full-time residents
- Identify tax structures that promote residency in the City

Task Setting
The committee identified the following tasks to be completed:

Committee Task	Status as of March 2022
Review existing exemptions for updates as appropriate	Partially complete
Review case studies of homestead exemption and other property tax structures	Complete

Review of the Property Tax Process
The committee confirmed all members' understanding of the annual process by which the tax rates and tax bills are determined.

The City of Newport's tax rates (a/k/a millage or "mill" rates) for Residential and Commercial properties are determined annually by dividing the total amount of the City's budget to be raised from property taxes (this amount is called the "levy") by the amount of certified value of taxable properties in each classification. Municipalities with more than one tax classification/rate, such as Newport's "Residential" and "Commercial" rates, must ensure that no rate may be greater than 150% of the lowest rate per state law. In calculating the annual tax rate, the City currently intentionally maximizes the Commercial rate at 150% of the Residential rate.

FY2022 City Budget (General Fund): $100,699,604

Revenues to be Raised by Property Tax: $ 79,768,850

Total Assessed Value of Residential Properties	$6,523,925,000 * $9.33 per $1,000 of value
Total Assessed Value of Commercial Properties	$1,202,813,000 * $13.99 per $1,000 of value
Total Assessed Value of Personal Property Other	$ 148,197,000 * $13.99 per $1,000 of value
	= $79,768,850

Each property's tax bill is determined by the following formula:

Property Assessed Value ÷ 1,000 x Residential or Commercial Tax Rate = Annual Tax Due

All properties undergo a full revaluation every nine years, most recently at 12/31/2020, and a statistical re-valuation every three years.

Review of Existing Property Tax Programs in the City of Newport

The City of Newport currently has in effect a number of programs for eligible residents to receive relief on their property tax bill. Nine of these programs are structured as "exemptions," meaning that a Property Assessed Value is reduced by *either* a preset dollar amount *or* a percentage of the Property Assessed Value. The table below lists each program, the number of enrolled properties during 2021, the type and amount of exemption and the impact to property value and tax bill for a sample property with a tax assessment of $500,000 under Newport's current residential tax rate of $9.33.

Existing Exemption Programs				Example for Property Assessed at $500,000			
Program Eligibility	# of properties enrolled for TY 2021*	Type of Exemption	Amount Discounted	Annual Tax Bill without Exemption	Taxable Value after Exemption	Annual Tax Bill with Exemption	Annual Savings on Bill
Senior, Income Qualified**	72	% of value	20%	$4,665	$400,000	$3,732	-$933
POW	0	set dollar amount	$52,000	$4,665	$448,000	$4,180	-$485
Vet Special Housing	1	% of value	10%	$4,665	$450,000	$4,199	-$467
Blind	14	set dollar amount	$39,800	$4,665	$460,200	$4,294	-$371
Veteran	441	set dollar amount	$21,400	$4,665	$478,600	$4,465	-$200
Widow(er)	132	set dollar amount	$21,400	$4,665	$478,600	$4,465	-$200
100% Disabled	31	set dollar amount	$18,000	$4,665	$482,000	$4,497	-$168
Gold Star Parent	0	set dollar amount	$3,000	$4,665	$497,000	$4,637	-$28
Discretionary for Infirmity or Poverty	32	assessor's discretion	assessor's discretion	$4,665	$0	$0	-$4,665

* Please note that properties can qualify for more than one exemption program

** Income qualification for the July 2022 billing cycle is $35,350 for single and $40,400 for married; these values are roughly 50% of FY21 HUD Area Median Income (AMI).

Additionally, the City offers a tax *deferral* program through which qualified properties may defer either fifty or one hundred percent of their annual tax bill due and continue the deferral by annual reapplication. It should be noted that there are currently no properties enrolled in the tax deferral program.

> The tax deferral program does not discount the property value or the resulting tax bill; it simply allows the homeowner to defer payment in exchange for a tax lien being placed on the home for the amount due. The property owner may continue to defer their tax liability with annual re-application and up until a total tax deferred of half of the assessed value of the home. Eligibility for this program is limited to residents age 65+ with primary domicile in Newport and with annual income below a "low income" threshold (same income limit as the Senior, Income Qualified exemption program). Additionally, properties only qualify if their assessed value is below the average recorded residential sale price for the prior year for the property type (condo, single family, etc). A full detailing of eligibility criteria can be found in the City ordinances 4.08.020 – Deferrals-Conditions.

As of the writing of this Interim Report, the Ad Hoc Tax Relief Committee has completed a review of the existing exemption programs above but has not discussed whether their eligibility or other criteria should be updated. Instead, the committee has spent the bulk of time focused first evaluating whether the Homestead Exemption or other structures should be deployed in the City.

The City of Newport currently has in its ordinances a Homestead Exemption program. The exemption was structured and approved by the City Council in 2002 but has never been utilized. The mechanics of the Homestead Exemption (in Section 4.08.140 of the City's ordinances) work the same way as the other exemptions above; that is to say, the exemption reduces the taxable value of the property. The ordinance, as currently structured, would allow for the Council to annually fix an amount of exemption of up to the following amounts:

- 35% for single-family and condominium properties
- 20% for two-family properties
- 5% for three-family properties

The ordinance does not currently include rules and regulations governing eligibility for the exemption, instead stating that "the city council shall provide by resolution or ordinance, rules and regulations governing eligibility for the exemption".

State Enabling Legislation
Implementation of exemption programs or changes to the tax classifications (e.g. Residential, Commercial, etc.) in a municipality require approval from the state legislature. The City of Newport would not have to pursue state approval to use the existing Homestead Exemption or refine the language in the ordinance, but the proposed adoption of any other structure will require following the process for seeking state approval.

Case Study Review
The committee researched and reviewed a wide variety of exemption and other property tax relief structures in effect throughout Rhode Island and select examples from across the country.

The following table includes a list of homestead exemption programs in effect in the state of Rhode Island:

Homestead Exemption Programs in Rhode Island				Example for Residential Property Assessed at $500,000			
City / Town	Type of Exemption	Amount Discounted	Resi Rate (TY2020)	Annual Tax Bill without Exemption	Taxable Value after Exemption	Annual Tax Bill with Exemption	Annual Savings on Bill
Narragansett	% of value	10%	$10.48	$5,240	$450,000	$4,716	-$524
East Providence	% of value	14%	$20.59	$10,295	$430,000	$8,854	-$1,441
Johnston	% of value	up to 20%	$20.59	$10,295	$400,000	$8,236	-$2,059
North Providence	% of value	20%	$22.81	$11,405	$400,000	$9,124	-$2,281
Woonsocket	% of value	25%	$24.00	$12,000	$375,000	$9,000	-$3,000
West Greenwich	% of value	29%	$23.79	$11,895	$355,000	$8,445	-$3,450
Lincoln	% of value	35%	$20.14	$10,070	$325,000	$6,546	-$3,525
Providence	% of value	40%	$24.56	$12,280	$300,000	$7,368	-$4,912
Central Falls	set dollar amount	$60,000	$23.69	$11,845	$440,000	$10,424	-$1,421

The committee noted that the difference between all qualified properties receiving a certain percentage – say 10% as in Narragansett RI – off of their property valuation results in smaller homes receiving a smaller deduction and larger homes receiving a larger deduction. Alternatively, if the exemption amount is a set dollar amount, for example either Newport's veteran's exemption at $21,400 or the Central Falls homestead exemption at $60,000; this is considered more optimal since it is more meaningful to owners of lower valued homes, but it raises the question of the need to update the value periodically to ensure it is at an appropriate level based upon inflation and real estate market conditions.

After having reviewed a number of these Rhode Island program examples, the committee was made aware of the recent publication of a report by the Lincoln Institute of Land Policy, titled "*Property Tax Relief for Homeowners*" (2021), which outlined a number of property tax relief programs in effect throughout the country (a copy of the report is enclosed with this memo). The report discusses the importance of the property tax to municipalities, comprehensively reviews common property tax relief programs and highlights some of their strengths and weaknesses. Upon review of the report, the committee was most interested in the homestead exemption model employed by the City of Boston, MA. The Boston program includes a unique feature to resolve the dilemma described above wherein an exemption that is set at a percentage of the value provides a lesser benefit to lower valued properties, while a fixed dollar amount needs to be updated periodically. The mechanism used in Boston is to annually calculate a dollar amount that all qualified properties receive as an exemption by first identifying the average value of all residential properties in the City, then taking 35% of that value and applying that dollar value as an exemption off the value of each qualified property.

Please also note that Boston pairs their homestead exemption program with a tax classification program, the importance of which will be discussed again further on.

Impact Evaluation of Exemption Programs

It is important to note that none of the property tax relief models contemplated by the committee and discussed in this report reduce the total amount of revenue raised from property taxes to support the City's budget.

A fundamental characteristic of any exemption program is that the reduction in available taxable value will cause an increase in the mill rate subsequent to implementation (assuming the same amount or greater of revenue to be raised from taxes). In other words, if one of the variables to the levy is reduced (the taxable value of property in the City), the other variable must increase to compensate for it (the property tax rate).

The committee learned that under the Narragansett RI model, for example, this had the effect of diluting the intended impact of the program and was confusing to the property owners, since when rates rose to compensate for the reduced taxable value overall bills did not decrease as much as was expected. The committee reviewed a model scenario in which Narragansett's program was hypothetically applied to Newport, using assumptions about the number and value of enrolled properties. Upon reviewing the model, the committee immediately observed that both Newport's residential and commercial tax rates were increased. Committee members felt strongly that an increase to the commercial tax rate was an unintended consequence of that model. In particular, it was noted that increased property tax expenses would negatively affect a commercial property's annual operating profit, which is a primary driver of valuation itself for commercial properties.

The Boston homestead exemption program also has the effect of increasing the millage rates. However, the Boston program uses an additional mechanism to insulate the commercial millage rates from the increase. "This is done by first allocating the tax levy across the city's four property classes based on their full value without any homestead exemptions. The residential tax rate is then calculated on the basis of net residential value." Therefore, the full effect of the increase in millage rate necessary to compensate for the decrease in available taxable value is applied within the residential tax rate. The result is that under the Boston program, the millage rate would increase to an even further degree than the Narragansett program. However, it should be noted that Boston has a relatively higher exemption rate at 35% than Narragansett at 10%, for example.

Recommendation to the Council

Thus far the committee had established that tax exemptions increase the millage rate, but that the increase to the millage rate could be isolated from the other tax classifications such as the commercial rate with the addition of a targeted mechanism. In response to the committee's:

(1) interest in the Boston homestead exemption model with its annual process of calculating the exemption amount,
(2) desire to insulate the City's commercial property rate from change and
(3) concern that allowing the qualified properties' residential millage rate to increase was confusing to property owners, as occurred in the Narragansett model

the committee has identified a model that aligns with the committee's goals by bifurcating the residential tax rate into "qualified" and "non-qualified" rates. This model would require state approval to obtain this further segmentation of the tax classifications currently held by the City of Newport.

The committee's recommended model ultimately provides qualified residential properties with an exemption without causing qualified properties' millage rates to increase, isolates the commercial rate from change, and calculates a higher rate to be charged to non-qualified residential properties by calculating the non-qualified rate based upon the portion of the levy to be raised from residential properties, net of the portion of the levy that will be paid by qualified properties after their exemption.

The committee has reviewed this model extensively, including a sensitivity analysis of the impacts of different rates of enrollment and/or different percentage rates of exemption. The committee has found this model to be the most promising in achieving the committee's stated goals. The annual process for implementing the program would be as follows:

(1) tax rates for residential and commercial property classifications would be calculated as if there were no bifurcation ("base rates")
(2) the annual amount to be exempted from qualified properties would be determined by calculating the average residential assessment and multiplying it by the rate of exemption decided upon by the Council (e.g. 10%, 20%, etc)
(3) then, the amount of levy to be raised from the qualified properties would be determined using the "base" residential rate multiplied by the net assessed values of qualified properties
(4) this calculated amount of the levy to be raised from the qualified properties, as well as the amount of the levy to be raised from commercial and other property, would be netted out of the total levy, with the balance of the levy being identified as the funds needed to be raised from the non-qualified residential properties
(5) per the normal procedure for calculating millage rates, the funds needed to be raised from the non-qualified residential properties would be divided by the total taxable value of those same properties in order to identify the "non-qualified" residential rate

Since the model calculates a flat dollar value that is discounted from qualified properties' taxable value, the tax is more meaningful to owners of lower value qualified residential properties and less meaningful to owners of higher value qualified residential properties. The following table illustrates the percentage change to tax bills for qualified properties under a number of different scenarios. It should be noted that the percent of taxable value to be discounted for qualified properties can be determined at a future point in time based upon further discussion of the committee and the Council.

Decrease (%) to Tax Bill of a Qualified Residential Property

	% of Average Value Discounted		
Value	**10%**	**20%**	**30%**
$300,000	-24%	-49%	-73%
$500,000	-15%	-29%	-44%
$750,000	-10%	-20%	-29%
$1,000,000	-7%	-15%	-22%
$1,250,000	-6%	-12%	-18%
$1,500,000	-5%	-10%	-15%
$1,750,000	-4%	-8%	-13%
$2,000,000	-4%	-7%	-11%
$5,000,000	-1%	-3%	-4%

Since the model calculates a higher tax rate to be applied to non-qualified residential properties, each non-qualified property experiences the same percentage increase in their tax bill. The following table illustrates what that percentage increase to all non-qualified residential bills would be in a variety of different scenarios (again, final program parameters would be set by the Council subsequent to state approval of the legislative change needed).

Increase (%) to Tax Bill of a Non Qualified Residential Property

	% properties Qualified		
Qualified Exemption	**40%**	**50%**	**60%**
10%	+5.2%	+8.2%	+12.7%
20%	+11.7%	+17.9%	+27.3%
30%	+18.2%	+27.6%	+41.8%

Additional Considerations

The committee notes that the Town Council of Middletown, RI recently adopted a resolution seeking a similar bifurcation, or "split," of the Town's residential tax classification. The committee reviewed the Town's resolution and presentation of the intended effects of the model from the Town Administrator. The Middletown model is best described as a "pure" split rate program, as compared to the hybrid model recommended by this committee. Under the Middletown model, the ordinance is crafted to allow the Town Council to determine the relative difference between the bifurcated owner-occupied and non-owner occupied rates, and qualified properties would be charged the lower rate and non-qualified properties would be charged the higher rate. The committee has identified two effects of this program that are not in alignment with the committee's goals:

(1) because the effect on property tax bills for both qualified and non-qualified properties would be driven only by a change in the rate, qualified property tax bills for lower value properties would receive a less meaningful discount, by dollar value, than higher value properties
(2) the eligibility for qualification for the lower tax rate only includes owner-occupied properties, which will have the effect of raising tax bills on rental properties without any differentiation between annually leased properties versus seasonal or short term rentals. The increased tax bill may be passed along to a tenant or may incent a landlord to change from an annual lease to a seasonal or short term leasing model.

Given the much higher prevalence of rental property throughout Newport as compared to Middletown, the committee would highly recommend to the Council the adoption of eligibility criteria to allow properties providing evidence of an annual lease to qualify for the lower residential tax rate. The committee has asked the City Solicitor to seek the most flexibility in the enabling legislation in order to allow the Council to make the final determinations with regard to eligibility.

THE CITY OF NEWPORT

RESOLUTION
OF THE
COUNCIL

No.2021-49

WHEREAS: the General Assembly has authorized the City of Newport pursuant to section 44-5-78 GLRI to annually fix a Homestead Exemption for taxable real property used for residential purposes; AND

WHEREAS: pursuant to the provisions of sections 44-5-76.1, 44-5-76.2 and 44-5-76.3 GLRI, the City has adopted a property tax classification system whereby residential real estate with less than four (4) units may be taxed at a lower rate than commercial properties; AND

WHEREAS: the City is also authorized to fix other real estate tax exemptions including exemptions based on age and disability to Newport residents who own and occupy residential property; AND

WHEREAS: in order to provide real estate tax relief to Newport residents, the City must be specifically enabled to provide the contemplated relief by an act of the General Assembly; AND

WHEREAS: on June 24, 2020 the Newport City Council passed a resolution directing the City administration to prepare options for implementing a homestead exemption in Newport; AND

WHEREAS: a workshop on homestead exemptions was held on March 18, 2021; AND

WHEREAS: this workshop showed a need to further review and investigate the homestead exemption, classification system and other measures to provide property tax relief to Newport residents, and to establish goals for the same and recommendations to achieve the same; NOW, THEREFORE BE IT

RESOLVED: the City Council shall create a Taxation Relief Ad-Hoc Committee; AND BE IT FURTHER

RESOLVED: this committee shall further review and investigate property tax relief for Newport residents and be comprised of members of the City administration who are familiar with taxation and exemptions and five members of the community, all who have a background in, and knowledge of finance, and preferably familiar with municipal property taxation.
This committee shall have the authority to hold meetings, conduct interviews, collect data, review ordinances and plans established by other communities and shall formulate a report to the Council with its findings and recommendations. The Committee shall have six months to perform this service and to present the council with its report.

Angela McCalla

IN COUNCIL
READ AND PASSED
JUNE 9, 2021

Laura C. Swistak
LAURA C. SWISTAK
CITY CLERK