Government of the District of Columbia
Office of the Chief Financial Officer

Jeffrey S. DeWitt
Chief Financial Officer

MEMORANDUM

TO:	**The Honorable Phil Mendelson** **Chairman, Council of the District of Columbia**
FROM:	**Jeffrey S. DeWitt** **Chief Financial Officer**
DATE:	**November 23, 2016**
SUBJECT:	**Fiscal Impact Statement – Four-unit Rental Housing Tenant Grandfathering Amendment Act of 2016**
REFERENCE:	**Bill 21-885, Draft Committee Print sent to the Office of Revenue Analysis on November 22, 2016**

Conclusion

Funds are not sufficient in the fiscal year 2017 through fiscal year 2020 budget and financial plan to implement the bill. The bill will cost $26,000 to implement in fiscal year 2017, and $175,000 over the four-year budget and financial plan.

Background

The bill requires[1] rental housing to remain under rent control if four or fewer rent-controlled units are transferred to a new owner via an intra-family transfer, or any other transfer exempt from the Tenant Opportunity to Purchase Act (TOPA). Transfers exempt from TOPA include transfers between spouses, parent and child, siblings, grandparent and grandchild, or domestic partners; transfers by a decedent's estate to members of the decedent's family; bankruptcy sales; transfers of bare legal title into a revocable trust; and other similar types of transfers. Currently, if four or fewer rent-controlled units are transferred to a new owner, and the total units owned by the new owner remains fewer than five, the transferred units are no longer subject to rent control.

For rent control to continue to apply to a unit after a TOPA-exempt transfer, the tenant of the unit must have lived in the building for at least 90 days prior to the transfer. Once the tenant leaves the unit, rent control no longer applies, and the new owner is allowed to raise the rent beyond the rent control ceiling.

[1] By amending Section 205 of the Rental Housing Act of 1985, effective July 17, 1985 (D.C. Law 6-10; D.C. Official Code § 42-3502.05)

Financial Plan Impact

Funds are not sufficient in the fiscal year 2017 through fiscal year 2020 budget and financial plan to implement the bill. The bill will cost $26,000 to implement in fiscal year 2017, and $175,000 over the four-year budget and financial plan.

Requiring certain properties to remain under rent control after they are transferred, means landlords of these properties might be required to charge rents lower than the market rate. The forgone rental income would lead to forgone revenue for the property tax[2] and the tax on rental income[3], since the value of the property would have likely increased after the transfer if the landlord had been able to increase the rent to the market rate.

We estimate there are about 20 property transfers a year that result in buildings of four or fewer units being taken out of rent control[4]. Cases that are known to us indicate that the rent increase could be up to 30 percent after the transfer. If the new owners of these properties were required to keep rent at rent-controlled levels, we would expect to see a total loss in property taxes of up to $29,000[5], and a total loss of rental income taxes of up to $11,000[6], in FY 2017 (the costs we list for FY 2017 in the table below are two-thirds of these total-year costs, since we would expect the legislation to take effect in February 2017, a third of the way through the fiscal year). The loss in taxes would increase each year since we would expect rental rates for non-rent-controlled properties to increase faster than the rates charged for rent-controlled properties.[7]

If the renters of these properties took the money they saved from rent control and spent it on taxable goods and services, we could see an increase in tax revenue that would offset some of the property and rental income tax losses. In fact, if renters saved about $200 a month, which we think is plausible, and spent it entirely on goods subject to the sales tax of 5.75 percent, the increase in sales tax revenue would be about equal to the loss in in rental income tax revenue that we project. However, because we cannot predict what renters will do with their savings, we are not incorporating increases in tax revenue into our fiscal impact of the bill.

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[2] A tax of 0.85 percent for residential real property, including multifamily properties.
[3] The unincorporated business franchise tax or the corporate franchise tax, one of which a landlord in D.C. must pay if the landlord's gross receipts total more than $12,000. The tax is currently 9.2 percent and will drop to 9.0 percent starting January 2017.
[4] Our property sales data suggests there are up to 200 apartment buildings with four or fewer units that are transferred each year and are exempt from TOPA. We assume that 10 percent of these buildings would have been subject to rent control before the transfer and would see a rent increase above rent control limits after the transfer.
[5] Assuming average annual property tax liability would have increased from $4,850 to $6,300 for each transferred building, had there been no rent control limit. This assumes that a 30 percent increase in rent would lead to a 30 percent increase in the value of the property. In our experience, the 30 percent increase in the property value is likely the upper limit of such an increase, since usually the percent increase in property value is less than the percent increase in rent.
[6] Assumes the average annual gross income for each transferred building would have increased from $37,000 a year to $48,000 a year, had there been no rent control limit.
[7] We assume that rent for non-rent-controlled properties will increase 5 percent a year, and rent for rent-controlled properties will increase 3 percent a year.

Cost of Implementing the Four-unit Rental Housing Tenant Grandfathering Amendment Act of 2016, FY 2017 to FY 2020					
	FY 2017	**FY 2018**	**FY 2019**	**FY 2020**	**Four-Year Total**
Property tax loss	$19,000	$32,000	$36,000	$40,000	$127,000
Rental income tax loss	$7,000	$12,000	$14,000	$15,000	$48,000
TOTAL COST	**$26,000**	**$44,000**	**$50,000**	**$55,000**	**$175,000**

Assumptions:
- About 20 apartment buildings with 4 units or less would be affected by this legislation each year.
- Extending rent control would reduce the total property tax revenue for these properties from about $126,000 to $97,000 in FY 2017.
- Extending rent control would reduce the total rental income tax revenue for these properties from about $39,000 to $28,000 in FY 2017. We assume the landlords will have gross receipts greater than $12,000 a year, which will make their rental income subject to the 9.0 percent corporate franchise tax or unincorporated business franchise tax.
- FY 2017 costs are prorated for two-thirds of the fiscal year, because we assume the legislation would not go into effect until February 2017.
- Costs in out-years increase because we assume that under rent control, the rents for these properties would increase on average by 3 percent a year, and without rent control they would increase, on average, by 5 percent a year.